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UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

In re	:	Chapter 11
MF GLOBAL HOLDINGS LTD., *et al*.,	:	Case No. 11-15059 (MG)
Debtors.	:	(Jointly Administered)
	:	

REPORT OF INVESTIGATION OF LOUIS J. FREEH,
CHAPTER 11 TRUSTEE OF MF GLOBAL HOLDINGS LTD., *et al*.,

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Louis J. Freeh (the "**Trustee**"), as Chapter 11 Trustee of MF Global Holdings Ltd. ("**Holdings Ltd.**"), MF Global Finance USA, Inc. ("**FinCo**"), MF Global Capital LLC ("**Capital**"), MF Global FX Clear LLC ("**FX Clear**"), MF Global Market Services LLC ("**Market Services**"), and MF Global Holdings USA Inc. (individually, "**Holdings USA,**" and collectively with Holdings Ltd., FinCo, Capital, FX Clear and Market Services, the "**Debtors,**" and collectively with their worldwide affiliates and subsidiaries "**MF Global**" or the "**Company**"),[1] respectfully submits this Report of Investigation (the "**Report**").

By orders dated November 28, 2011 [Docket No. 170], December 27, 2011 [Docket No. 306], and March 8, 2012 [Docket No. 548], the Court appointed the Trustee to serve as Chapter 11 Trustee. Sections 1106(a)(3) and (a)(4)(A) of the Bankruptcy code require the Trustee to:

> . . . investigate the acts, conduct, assets, liabilities, and financial condition of the debtor, the operation of the debtor's business and the desirability of the continuance of such business, and any other matter relevant to the case or to the formulation of a plan;
>
> . . . including any fact ascertained pertaining to fraud, dishonesty, incompetence, misconduct, mismanagement, or irregularity in the management of the affairs of the debtor, or to a cause of action available to the estate.

11 U.S.C §§ 1106(a)(3) and (4). Accordingly, the Trustee has a duty to investigate and, if necessary, bring any claim available to the Debtors' estates, including, without limitation, claims against current and former officers and directors of the Company. The Bankruptcy code also requires that the Trustee "file a statement of any investigation conducted" under 1106(a)(3). 11 U.S.C. § 1106(a)(4)(A).

[1] An organizational chart of the companies comprising MF Global is attached as Appendix A.

This Report is based on interviews of former employees of MF Global and former members of the Holdings Ltd. Board of Directors (the "**Board**") conducted by the Trustee's counsel, the review of hundreds of thousands of documents and other materials available to the Trustee, and forensic investigation conducted by the Trustee's professionals, including FTI Consulting, Inc. ("**FTI**"), the Trustee's financial advisors.

Although the Trustee, his professionals, and the Debtors' estates have cooperated with the various law enforcement and regulatory agencies investigating MF Global's collapse, the Trustee has no law enforcement or regulatory authority, did not participate in the interviews conducted as part of law enforcement and regulatory investigations, and has not been included in those investigations. Rather, the Trustee has deployed his professionals and the Debtors' limited resources to review the most relevant information in order to complete his investigation and issue this Report in an efficient manner. This Report represents the best information available to the Trustee at this time, and may be supplemented or updated in the event that new or additional information is identified or brought to the Trustee's attention.

This Report reflects the Trustee's findings and focuses on the underlying causes of the collapse of the Company, as well as the roles and actions of current and former officers and directors. Although the Report includes some discussion of the alleged shortfall of segregated customer funds at MF Global, Inc. ("**MFGI**"), an indirect subsidiary of Holdings Ltd., announced on October 31, 2011, the recovery of those funds falls outside the scope of the Trustee's authority and, therefore, the cause of that shortfall is not the focus of this Report.[2]

[2] As described in the *Plan Proponents' Motion to (i) Approve the Disclosure Statement Supplement, (ii) Approve Expedited Solicitation Procedures with Respect to the Disclosure Statement Supplement and Plan Adjustment, and (iii) Grant Related Relief* [Docket No. 1182], the Trustee believes the alleged shortfall is likely to be between $6 million and a possible surplus of $120 million.

I. EXECUTIVE SUMMARY

Prior to the Debtors' bankruptcy filings, MF Global, through its regulated and unregulated broker/dealers ("**B/D**") and futures commission merchant ("**FCM**"), was a leading brokerage firm offering customized solutions in the global cash and derivatives markets.[3] MF Global provided execution and clearing services for products in the exchange-traded and over-the-counter derivatives markets, as well as for certain products in the cash market. MF Global was headquartered in the United States and conducted operations in, among other locations, the United Kingdom, France, Singapore, Australia, Hong Kong, Canada, India and Japan.

Jon Corzine ("**Corzine**") was named the Chief Executive Officer ("**CEO**") and Chairman of the Board of Directors ("**Chairman**") in March 2010, at a time when the Company's future was in doubt. The Company's traditional commodities and securities broker business earned revenues primarily (1) through commissions earned from executing customer orders, and (2) from interest earned on customer funds and from its matched repo book. In an environment of historically low interest rates, that model failed to be profitable. At the time Corzine joined MF Global, credit rating agencies were threatening to further downgrade the Company unless it increased its revenues and earnings.

Corzine embarked on a mission to transform the Company into a full-service B/D and investment bank. In order to increase revenues, and to support the Company during a period of expanding the business, the Company began, for the first time in its history, to engage in significant proprietary trading (*i.e.*, using the Company's own funds to trade for the Company's

[3] A list of officers, directors, and key employees is attached as Appendix B.

benefit in order to profit from anticipated changes in market prices), directly under Corzine's supervision. Although the Company had previously taken positions in sovereign debt and had engaged in repurchase to maturity trades, Corzine initiated a new and aggressive trading strategy, investing heavily in European sovereign debt, which was financed through repurchase to maturity transactions (the "**Euro RTMs**").

MFGI and MF Global U.K. Limited ("**MFG UK**") were the MF Global entities that directly engaged in the Euro RTMs. MFGI would purchase securities, and MFG UK acted as agent for the purchase because it was the only MF Global entity that was a member of the clearinghouses in Europe.

One of the principal advantages of the Euro RTMs was their accounting treatment. Because of the way these trades were structured, the Company immediately recognized the income while simultaneously removing the transactions from the Company's balance sheet. These transactions were meant to serve as a profit "bridge" until the Company began to produce earnings from other, new lines of business, at a time when, as Corzine stressed during an earnings call in August 2010, "[e]arnings, earnings, earnings continue[d] to be the mantra and the task at hand."

The Euro RTMs involved financing the Company's purchase of European sovereign debt, issued by countries such as Italy, Portugal, Spain, and Ireland (collectively referred to as "**IPSI**"). The transactions were intended to capitalize on volatility and unrest in the European markets.[4] Although the transactions were fully financed, the clearinghouses required a payment

[4] On June 3, 2010, Corzine told an industry audience: "I just heard that market volatility is our friend. I believe that also . . . . [T]here is a tremendous opportunity in the marketplace on this natural course of restructuring that will be going on in the nation, in our companies, and frankly across the globe."

of margin in the form of cash or other acceptable collateral at the time the transaction was executed ("**Initial Margin**"). MFGI, through its agent, MFG UK, also was subject to additional margin based upon a variety of factors ("**Variation Margin**"). Initial Margin could vary based on the credit quality of the counterparty, the credit quality of the issuer, and the maturity and duration of the bond. Variation Margin was based on market factors, such as price movements in the underlying sovereign bonds. Under stressed financial conditions, the Initial and Variation Margin demands could increase dramatically, with additional new Variation Margin required as a result of, among other things, adverse price movements in the value of the underlying European sovereign bonds.

When combined with other factors, strategic decisions and management lapses surrounding the Company's business, the Euro RTMs ultimately sowed the seeds of the Company's destruction. Although the trades generated the expected up-front "income," these trades also jeopardized the Company's available liquidity and left the Company highly leveraged as a result of these off-balance sheet transactions. When the European economy deteriorated during the summer of 2011, clearinghouses and other counterparties began making escalating margin demands, draining the Company's liquidity and drawing the attention of regulators and credit rating agencies.

Between September 2010 and June 2011, the Board approved a series of requests initiated by Corzine to increase the risk limits for investing in European sovereign debt. The Board gave these approvals only after the Holdings Ltd. Chief Financial Officer ("**CFO**") and other managers provided assurances that MF Global had sufficient liquidity, even under various stress scenarios, to satisfy any current or projected margin demands.

During the summer of 2011, the Chief Risk Officer ("**CRO**"), Michael Stockman ("**Stockman**"), recommended that MF Global stop investing in Euro RTMs, and start hedging its existing exposure. Despite this advice, rather than cease or limit its investments in Euro RTMs, management searched for additional sources of liquidity to support the Company's trading strategy. At one point, management even debated how aggressively the B/D, on an intraday basis, could borrow FCM customer funds required to be kept in secured and segregated accounts.

As these events unfolded, Corzine and his management team failed to strengthen the Company's weak control environment, making it almost impossible to properly monitor the liquidity drains on the Company caused by Corzine's proprietary trading strategy. Among other significant gaps, the Company lacked an integrated global treasury system, preventing management from obtaining an accurate real-time picture of the Company's liquidity. The inadequate controls also prevented the Company from knowing, during the last week of its existence, that customer segregated funds at the FCM were being used to meet the B/D's liquidity needs and satisfy an obligation of MFG UK.[5] These glaring deficiencies were long-known to Corzine and management, yet they failed to implement sufficient corrective measures promptly.

In late October 2011, the Company announced substantial quarterly losses and additional credit rating downgrades. Subsequent MFGI customer withdrawals and losses on sales of assets, coupled with the Company's inadequate controls and weak liquidity position and other factors,

[5] In testimony before the House Committee on Agriculture on December 8, 2011, Terrence Duffy, Executive Chairman of CME Group Inc., stated that was the first time in history that a shortfall in customer segregated funds occurred as a result of the clearing member's improper handling of customer funds and the first time in history that a customer suffered a loss as a result of such improper handling of customer funds.

significantly impaired the Company's ability to pay its debts as they came due, until the Company's only means of survival was for Holdings Ltd. to sell its assets to another company. However, a deal to avert bankruptcy through such a sale collapsed at the eleventh hour when the FCM identified a substantial unexplained shortfall in customer segregated funds. When efforts to sell the business failed, Holdings Ltd. was left with no choice but to file for bankruptcy protection for itself and FinCo.

The negligent conduct identified in this Report foreseeably contributed to MF Global's collapse and the Debtors' subsequent bankruptcy filings. Although a difficult economic climate and other factors may have accelerated the Company's failure, the risky business strategy engineered and executed by Corzine and other officers and their failure to improve the Company's inadequate systems and procedures so that the Company could accommodate that business strategy contributed to the Company's collapse during the last week of October 2011.

II. FACTUAL BACKGROUND

A. Transformation into MF Global

In November 2005, Man Group plc ("**Man Group"**), a publicly-traded company that traced its origins to the 1700s, purchased client assets and accounts from Refco LLC ("**Refco**"), a New York-based financial services company, following Refco's collapse in the aftermath of an internal accounting fraud scandal. Through the acquisition of Refco's assets, Man Group took control of one of the largest brokers in the U.S. futures market.

Man Financial Inc. ("**Man Financial**") was Man Group's Chicago-based U.S. brokerage unit. At the time of the Refco purchase, Man Financial ranked as the ninth largest futures broker in the U.S. The Refco purchase gave Man Group and Man Financial a significantly stronger industry position in the U.S., as well as a much larger international footprint.

In 2007, Man Group separated the investment and brokerage sides of its businesses. Through a number of transactions, including an initial public offering ("**IPO**"), Man Group spun off Man Financial. The new entity was initially re-named MF Global Ltd. and, subsequently, MF Global Holdings Ltd. The IPO was announced on July 18, 2007 for 97.38 million shares that would trade on the New York Stock Exchange. Registration statements filed in connection with the IPO noted that Holdings Ltd. typically did not engage in directional or proprietary trading. When Holdings Ltd. did take proprietary positions, it did so "primarily on a matched-principal basis in response to client demand." Public filings also noted that by taking positions to facilitate client trades or to hedge or manage corporate assets, the Company had less exposure to market risk and cash liquidity risk. By the end of 2007, MF Global had a market cap of almost $3.8 billion.

B. The Dooley Incident and MF Global's Risk Infrastructure

Several months after Holdings Ltd. went public, MFGI experienced a massive financial loss as a direct result of misconduct by one of its employees in MFGI's Memphis, Tennessee branch office. During the night of February 26, 2008, an MFGI trader, Evan Dooley ("**Dooley**"), improperly established an excessive position in wheat futures. When the futures market swung against those positions the following morning, Dooley entered multiple large offsetting trades that MFGI, as a clearing member of the Chicago Mercantile Exchange ("**CME**"), was absolutely required to fund from its own accounts. The resultant overnight loss of over $141 million effectively eliminated most of the Company's profit for the year.

Dooley was able to establish excessive trading positions without MF Global's knowledge due to an error in the configuration of computerized position limits in MFGI's trading platform,

which deactivated automatic restrictions on Dooley's activity. No one at MF Global, including the Compliance and Risk Departments in its New York, Singapore, and London offices, detected Dooley's misconduct until mid-morning (EST) on February 27, 2008. By the time MFGI could respond by shutting Dooley out of its trading systems, all but 0.02% of the financial loss had already been incurred by MF Global.[6]

1. Immediate Impact of the Dooley Incident

MF Global suffered immediate and severe negative consequences from the Dooley incident. Holdings Ltd.'s share price declined significantly. Moody's Investor Service ("**Moody's**") downgraded Holdings Ltd.'s credit rating from A3 to Baa1 and Fitch Ratings ("**Fitch")** assigned a Negative Watch, signaling additional potential downgrades. Clients also withdrew assets from their MFGI accounts. As of March 31, 2008, client assets at MFGI were down $4.2 billion when compared to the previous quarter.

The Commodity Futures Trading Commission ("**CFTC**") also fined MFGI $10 million for poor risk management practices and ordered MFGI to implement certain undertakings and the recommendations of a consultant, Promontory Financial Group LLC ("**Promontory**"). Promontory made a number of recommendations, including that MF Global establish a global enterprise risk management framework, strengthen its operational risk management procedures, and enhance its supervision of trading desks.

The combined impact of the $141 million loss, the $10 million fine, and ongoing regulatory and civil litigation took a toll on the Company's financial health. In July 2008, the Company secured some relief when J.C. Flowers & Co. ("**J.C. Flowers**"), a private equity firm,

[6] In December 2012, Dooley pled guilty to two counts of exceeding government limits on speculative commodity trading in violation of the Commodities Exchange Act.

invested $150 million in Holdings Ltd. in exchange for preferred shares and a seat on the Board. David Schamis ("**Schamis**"), a managing director and member of J.C. Flowers's operating committee, held this Board seat until Holdings Ltd. and FinCo filed for bankruptcy.

2. Creation of the CRO Position

After the Dooley incident, the Company formally established the CRO position to exercise "control over MF Global's [Enterprise Risk Management] framework and [have] global responsibility for controlling credit, market, operational, concentration, capital, and liquidity risks." The CRO was given responsibility for providing the Board with comfort that MF Global had identified, assessed, measured, monitored, controlled and/or mitigated all of the Company's risks. The CRO initially had a direct reporting line to the CEO, and was also given direct access to the Board. The Company's first CRO, Michael Roseman ("**Roseman**"), was hired in August 2008.

3. Development of Written Policies Following the Dooley Incident

In the aftermath of the Dooley incident, the Company adopted a written framework for managing risk. This framework was never fully implemented.

a. Escalation Policy

In June 2009, the Board approved an Enterprise Risk Management Escalation Policy ("**Escalation Policy**"). The purpose of the Escalation Policy was to ensure that "knowledge of the incidents [was] disseminated to the appropriate authorized individuals in a timely manner." The Escalation Policy established a reporting chain, reporting protocols, and reporting timeframes for risk incidents.

Pursuant to the Escalation Policy, any capital or liquidity risk incidents were required to be escalated up a specific, identified reporting chain. Some examples of serious risks that

required immediate escalation included an external rating downgrade, a legal entity falling below the required regulatory capital minimum, or "unexpected events" resulting in available funds falling by more than 30 percent.

b. Risk Policy

In March 2010, the Board also approved an MF Global Enterprise Risk Policy ("**Risk Policy**"), which established a written control framework for managing the Company's risk.

The Risk Policy specifically identified liquidity risk as the "[r]isk that the [Company], although solvent, either (1) does not have available sufficient liquid financial resources to enable it to meet its obligations as they fall due or (2) can secure sufficient liquid financial resources only at an excessive cost."

The Risk Policy called for the creation of a new position in the Risk Department, a Global Head of Capital & Liquidity Risk, who would take responsibility for:

> independent and objective assessment of liquidity risk; reviewing liquidity scenario analyses conducted by [the] Treasury [Department], as well as risk scenarios conducted by other risk areas (*i.e.*, operational risk, credit risk, market risk) that may lead to liquidity events; monitoring liquidity against limits outlined in the Risk [Delegations of Authority]; and presenting independent liquidity-risk information and intelligence through the CRO to management and the Board.

The Global Head of Capital & Liquidity Risk also was responsible for monitoring MF Global's adherence to the Liquidity Risk Methodology Document (the "**LRMD,**" also referred to as the "Liquidity Risk Management Document").

The Company never hired a Global Head of Capital & Liquidity Risk, instead relying on existing personnel to perform the functions of this position on an inconsistent and ad hoc basis. As discussed further below, the Company also never adopted the LRMD.

The expected combined effect of the Risk Policy and the Escalation Policy was to establish a structure for managing various types of risk. The Risk Policy and Escalation Policy presented the framework by which the Company would oversee risk management activity and ensure that various risks were reported, through committees and other mechanisms, so that management could address those risks. Specifically, the policies provided for the creation of:

(1) an Enterprise Risk Management Committee ("**ERMC**") to "monitor risk-management activity across all of MF Global's risks and geographic locations," and to provide "a forum for Senior Management to discuss risks that affect the Company's strategic objectives, including any risks related to strategy implementation, new products or geographic locations, and mergers and acquisitions"; and

(2) an Asset/Liability Committee ("**ALCO**") responsible for ensuring that the overall mix of market, investment and liquidity risk within the asset/liability portfolio of MF Global and its subsidiaries was constantly managed within appropriate limits.

4. Implementation Failures

In the years between the Dooley incident and the Holdings Ltd. and FinCo bankruptcies, Corzine and his managers failed to implement many key measures required under the risk policies approved by the Board. These deficiencies are discussed in greater detail in Section III below, but some examples of the Company's implementation failures include:

(1) As early as May 2010, management was warned that the Company's Treasury Department lacked the appropriate systems and technology to conduct accurate, real-time liquidity monitoring and forecasting. Company policies required the Treasurer to "ensure that effective liquidity forecasting and cash management processes [were] in place, documented and functioning across MF Global, including specific processes to identify any expected cash items that remain outstanding and appropriate action to cover any shortfall." According to the Company's internal assessment, this was a "high" priority practice gap.

(2) The Company failed to develop the LRMD or the contingency funding plan required to assess potential liquidity requirements arising from adverse market or operational situations. The purpose of the LRMD was to memorialize "[t]he liquidity requirements derived, any operational effects on MF Global identified, the assumptions used and comments on the effectiveness of operational controls" to be communicated through the ALCO, the Enterprise Risk Management Committee and, ultimately, the Board.

(3) The Company did not conduct stress tests of its contingency funding planning arrangements. The Treasurer, the Global Head of Capital & Liquidity Risk (the position that was never filled) and the ALCO were responsible for considering "whether a test needs to be conducted to assess the effectiveness and completeness of the contingency arrangements detailed above in advance of having to implement them in an adverse liquidity situation." As a result of the failure to conduct tests, the Company failed to identify and correct problems that were revealed during the final weeks of the Company's existence, when acute liquidity stresses made it impossible for personnel in the Company's Operations Department to settle trades necessary to keep the Company afloat.

(4) The Risk Policy delegated to Internal Audit the responsibility to provide "independent assurance to the Audit Committee [of the Board] about the effectiveness and integrity of MF Global's risk framework, policies, and control infrastructure, and risk-policy application in the Company's day-to-day operations across all product types and geographic locations." The Company's Internal Audit Department ("**Internal Audit**") raised many action items as risks to the Company's business on consecutive Internal Audit reports, but the Company never addressed these items before it collapsed.

5. Promontory's Approval of Written Policies

On May 26, 2010, Promontory reported to the Audit and Risk Committee of the Board that MF Global had "successfully and effectively implemented" most of the CFTC undertakings

and Promontory recommendations made as a result of the Dooley incident. This included development of written policies (the Risk Policy, the Escalation Policy) and enhanced compliance programs and procedures. Promontory also approved upgrades made to the Risk Department's technology for monitoring and analyzing market and credit risk and its development of a stronger, more proactive internal auditing function.

However, the written policies that Promontory recommended and endorsed were never fully implemented, a fact that Corzine and management learned through reports prepared by Internal Audit that repeatedly listed implementation gaps in the Company's risk and control systems.

C. Corzine Joins MF Global as Chairman and CEO

Corzine was appointed as Chairman and CEO on March 23, 2010. Corzine replaced outgoing CEO Bernard Dan ("**Dan**"), who resigned abruptly earlier that year. Dan had served as CEO since October of 2008, when he replaced former CEO Kevin Davis, who had served as CEO of the Company's predecessor entity for 17 years. Dan's departure was sudden, leaving MF Global unexpectedly searching for a new CEO.

Corzine had previously served as Chairman and CEO of Goldman Sachs, as a United States Senator from New Jersey, and as Governor of New Jersey. Following defeat in his bid for re-election as Governor of New Jersey, Corzine joined J.C. Flowers as an operating partner, where Schamis was also a partner and managing director.

Schamis first told his fellow Board members about the possibility of approaching Corzine without identifying him by name. After Schamis discussed the opportunity with Corzine and Corzine expressed interest, Schamis identified Corzine to the Board. The Board was interested

in Corzine as either an interim or permanent CEO. Several Board members were pleasantly surprised that Corzine considered taking the position.

Discussions with Corzine moved very quickly after he was first approached. The day after Schamis's discussion with Corzine, Corzine met with a small group of Company personnel. The day after that, Corzine met with a larger group. By Friday of the same week, Corzine had agreed in principle to take the job. The Company announced his selection as the new CEO and Chairman the following Tuesday, March 23, 2010.

In September 2010, Corzine hired Bradley Abelow ("**Abelow**") as Chief Operating Officer ("**COO**"). Abelow had previously served as Corzine's Chief of Staff when he was the Governor of New Jersey and had been a partner at Goldman Sachs during Corzine's tenure there as Chairman.[7] Corzine began to rely more upon Henri Steenkamp ("**Steenkamp**"), then Chief Accounting Officer ("**CAO**"), even though Randy MacDonald ("**MacDonald**") remained the Company's official CFO until April 2011.[8] Kemper Cagney ("**Cagney**"), MFG UK's CFO, began reporting to Steenkamp instead of MacDonald.

Corzine was hired as both Chairman and CEO, positions that had historically been held at MF Global by two different individuals. The Board also appointed Corzine as chairman of the Executive Committee and reduced the committee's size from five to four members.

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[7] Corzine shared the news of Abelow's hiring with investors: "Today, there is an announcement out that we have hired Brad Abelow to come in as our Chief Operating Officer. Brad last worked with me as a state treasurer in New Jersey . . . but the fact is I think he's a very strong individual, was my chief of staff. Before that he was a partner at Goldman Sachs for about 15 years, ran our Asian operations and then the operations of the [Company]. We feel very strongly about his contribution to us going forward."

[8] When Corzine was approached about joining the Company, Steenkamp had flown immediately to New York from Singapore, in order to review the Company's numbers with him, whereas MacDonald had not returned from a vacation in Florida to meet with Corzine.

During Corzine's tenure as Chairman, the Board consisted of Corzine, David Bolger ("**Bolger**"), Eileen Fusco ("**Fusco**"), David Gelber ("**Gelber**"), Martin Glynn ("**Glynn**"), Edward Goldberg ("**Goldberg**"), Schamis, and Robert Sloan ("**Sloan**"). The Board operated with several committees.[9] Fusco was chair of the Audit and Risk Committee and the Supervisory Sub-Committee of the Audit and Risk Committee. Corzine served as chair of the Executive Committee. Gelber served as chair of the Compensation Committee. Bolger served as chair of the Nominating and Corporate Governance Committee. From time to time, as needed during various public offerings, the Board also organized a Pricing Committee chaired by Corzine.

1. Corzine's Plan to Transform the Company

When Corzine joined MF Global in March 2010, the Company was struggling. Moody's and Fitch had rated MF Global just two notches above junk status (Baa2 and BBB, respectively), and Standard & Poor's ("**S&P**") had rated MF Global just one notch above junk status (BBB-). The rating agencies quickly indicated to Corzine that they expected to see earnings increase or the Company would face additional downgrades.[10] Moody's specified a financial target of $200 to $300 million in annual pre-tax earnings for the Company to maintain a Baa2 credit rating. Moody's also indicated that it wanted to see a significant reduction in MF Global's balance sheet leverage.

[9] A list of the Board committees and the members of each committee is attached as Appendix C.

[10] MF Global conducted quarterly presentations for the credit rating agencies. The presentations were typically given by Steenkamp, MacDonald, or Corzine. During the period following Corzine's arrival at MF Global, the credit rating agencies warned the Company that if it continued to fail to generate revenues, it would be further downgraded. It would not be sufficient simply to reduce expenses. The rating agencies demanded revenue growth quarter after quarter to avoid a downgrade.

Corzine also articulated the need to increase earnings during a call with investors on May 20, 2010:

> One thing is for certain, the rating agencies expect us to produce earnings. I think every one of the reports underscores that as forcefully as I did in my remarks. We understand that. I think that the impermanency of capital is a question that any reasonable analyst, whether you are at a rating agency or an investor, would have on your question list, your to do list.

Corzine soon recognized that the Company's business model was untenable. The Company's traditional business model was to earn interest on the investment of client funds at market interest rates and commissions on trades. When Corzine joined the Company, this business model was struggling because of significantly lower interest rates and because client funds were not generating the levels of revenue they had in the past. Corzine quickly came to the conclusion that members of the Board had already reached: a voice-brokered FCM in a low interest market was a failing business model, especially when the chairman of the Federal Reserve Board predicted that interest rates would remain low for a number of years to come.

Given these difficulties, Corzine set out to diversify the Company's revenue streams. He began planning new lines of business to help the Company generate additional revenues by transforming the Company first into a B/D and eventually into a full-scale investment bank.

2. The Launch of Proprietary Trading

At least two Board members recalled discussing the idea of proprietary trading with Corzine either prior to or shortly after he joined the Company in March 2010.

During a May 20, 2010 earnings call, Corzine also described this vision of MF Global's future for investors. He noted that the Company's poor financial performance in the past was not acceptable and should not be tolerated by management or the Company's shareholders. He

indicated that, for the first time, MF Global would engage in proprietary trading across all product lines, explaining:

> Lastly, a natural extension of our existing approach to client services, which has traditionally been organized around an agency brokerage model, over the near term we will extend our client facilitation efforts to include principal risk taking across most product lines. Our Fixed Income and US Treasury businesses already incorporate this approach. It's clear to me that we can expand revenues meaningfully by this extension. We'll provide our clients with better market execution which in time will facilitate growth of client balances, derivative commissions and trading profits. **As we grow these activities we will be mindful of the necessity to enhance and reconfirm our operational and control functions and to secure the talent necessary to manage [attendant] market risks. I want to be clear. I don't anticipate increasing our current risk appetite in the near term but we will encourage facilitation desks to operate more aggressively within our existing limits.** Again, this intensity requires another element of cultural shift because we have often thought of simply agency business as the way we approach our clients.

(Emphasis added.) Corzine's strategy was that, in order to generate revenues, the Company needed to take on greater risk. In light of MF Global's previous risk-averse business culture, this was a significant change in the Company's direction.

3. The Hiring of Boston Consulting Group

After he had been with the Company for several months, Corzine announced to the Board that he had hired Boston Consulting Group ("**BCG**") to advise him on corporate strategy. BCG consulted on Corzine's plan during the summer of 2010. According to several former Board members and officers of the Company, BCG did not originate the business strategy. Instead, BCG was engaged as a consultant to evaluate Corzine's vision. During the summer of 2010, Corzine led a strategic review of the Company's business lines, considered a retail business plan,

reviewed the Company's institutional sales efforts, and gathered his thoughts on the Company's product lines and governance.

At a Board meeting on October 28, 2010, Corzine discussed his strategic vision and priorities. Among other things, he indicated that additional hires would be warranted given the greater focus on principal trading. Management was also meeting with the Federal Reserve at this time to continue discussions regarding the Company's application to become a primary dealer, which would allow the Company to trade U.S. government securities with the Federal Reserve Bank of New York ("**New York Fed**") and participate in U.S. Treasury auctions. At the same time, the Company also was preliminarily exploring capital raising opportunities. Corzine indicated that at the next Board meeting in December, he would discuss with the Board the Company's strategic plan based on, among other things, his tactical review of the Company since joining in March 2010.

At the December 15, 2010 Board meeting, representatives of BCG presented their final study to the Board (the "**BCG Presentation**"). The BCG Presentation listed the Company's strengths and challenges, discussed proposed short-term and long-term objectives, and the "strategic pillars for growth." The BCG Presentation stated that MF Global had made significant progress over the prior year in: (1) stabilizing its business through cleaning its balance sheet; (2) improving its capital structure; (3) reducing its workforce; and (4) strengthening its management team. But BCG also warned that the core broker business – primarily the FCM – continued to be fundamentally challenged by pricing pressure and competition from large investment banks with significantly more capital. BCG indicated that MF Global was at a crossroads and had to decide whether to evolve beyond its current "pure execution focus."

The solution: "MF Global [would] evolve from a broker to a [B/D] en route to becoming a full-service investment bank." BCG identified "five key strategic pillars" to this vision:

(1) strengthen the core brokering/execution business;

(2) extend into a B/D with increased risk-taking;

(3) consolidate and streamline retail offering;

(4) organize to take advantage of transaction services infrastructure; and

(5) diversify into commodities-based asset management.

One of several key initiatives BCG identified was the build-out of a "robust risk management infrastructure, including platforms, tools, policies, and procedures for both market making and principalling." BCG recommended shoring up operations and information technology and providing greater management information systems and transparency through tools and processes in the Finance Department. BCG identified infrastructure-related enhancements such as risk compliance and organizational restructuring as a priority for the strategic plan.

At the time, the credit rating agencies appeared to view Corzine's vision positively. However, their focus remained on improved earnings. To stave off a rating downgrade, Corzine promised that the Company would return to profitability in four to six quarters.[11]

[11] By February 2011, approximately a year after Corzine joined the Company, Moody's evaluated MF Global again. Moody's considered whether the Company could maintain liquidity and risk management discipline as it executed its new strategy. Moody's noted that "[g]aining market share — while maintaining a disciplined approach to risk — will be challenging because MF Global's strategy and aspirations are shared by the rest of the industry. Many of its competitors however, boast far greater capital, stronger brands, and a greater ability to attract and pay for talent."

4. Expansion of the Company's Trading Capabilities and Establishment of the Principal Strategies Group

To pursue his strategy, Corzine substantially expanded the Company's trading capabilities. MF Global hired mortgage and other brokers, obtained primary dealer status and considered acquiring a commodity pool business and other partnerships. The Company also consolidated its retail business under MacDonald, who was formally appointed as Global Head of Retail in December 2010.

Corzine hand-picked the traders with whom he worked, including Lauren Cantor ("**Cantor**"). Cantor originally was hired to establish interest rate derivative trading on the Company's primary dealer platform. Corzine asked Cantor, who had engaged in proprietary and client trading at other firms, to work directly with him. Cantor facilitated Corzine's trading and helped build the Company's proprietary trading platform. Cantor also opened new accounts in Corzine's name.

In June 2010, Corzine started trading on his own using an existing Treasury Department account. He maintained his own portfolio for the Company in accounts that bore his initials, JSC.

By the fall of 2010, MF Global established a proprietary trading unit at MFGI, the Principal Strategies Group (the "**PSG**"). The Company began to hire traders, analysts and associates to engage in proprietary trading in various product areas. From the outset, as Corzine told investors during an earnings conference call in November 2010, the Company sought to hire "the most successful and productive proprietary traders," and intended "to stay in high turnover mode within [its] proprietary activities." Until that time, MF Global did not have substantial

experience with proprietary trading. Corzine's expectation was that bringing these proprietary traders into the organization would "demonstrate not just . . . [the] success of the group, but that [the Company could] take and manage risks successful[ly] for purposes of generating revenue . . . ."

PSG initially consisted of six senior traders, three junior traders and a trading assistant. PSG's traders sat apart from the other traders (including those trading on behalf of MFGI's customers) and close to the offices of the Company's executive officers. The group relied on the existing "middle" and "back office" support staff for account setup and management processes, as well as clearing and settlement processes. Even as the Company went from doing little to no proprietary trading to engaging in proprietary trading in many asset classes by many different trading desks, management failed to increase the level of "back office" support staffing necessary to support this level and volume of trading.

Corzine's investment in new trading desks and product groups caused the Company to assume considerable up-front costs associated with the hiring of new traders and the establishment of new product lines. Management believed these expenditures were necessary to eventually develop the Company into an investment bank. In the early summer of 2010, Corzine also met with MF Global's senior traders to discuss ways to improve profitability and to address the rating agencies' continued demands for larger revenues.

One of the ideas generated in Corzine's discussions with senior traders was trading in the sovereign debt of economically distressed European countries such as the IPSI nations and Belgium. The Company had a history of trading in European sovereign debt before Corzine's arrival, but these positions were not structured as repurchase to maturity transactions, they were

relatively small (approximately $400 million), they were entered mainly to facilitate customer trades, and they could be liquidated easily. After his discussions with senior traders in the summer of 2010, Corzine became an advocate of investing in Euro RTMs.

5. Corzine's Trading Activities

Corzine spent a significant amount of time trading and overseeing PSG, even placing trades in the middle of meetings. The amount of time Corzine spent trading was a frequent topic of discussion among MF Global employees. Abelow and others questioned whether the Chairman and CEO should be so focused on trading, as opposed to the many other demands of his position.

Corzine's trading activities were only minimally supervised, and only to the extent that his direct role in trading implicated Rule 3012 of the Financial Industry Regulatory Authority ("**FINRA**"), which requires that all trading must be supervised by "a person who is either senior to, or independent of" the trading personnel.

To comply with the FINRA rule, management and the Board put into place certain procedures designed, at least in theory, to properly supervise Corzine and the trades placed through him. The Audit and Risk Committee established a special Supervisory Subcommittee to oversee Corzine's activities and delegated day-to-day supervision of Corzine to the Company's Chief Compliance Officer, Tracy Whille ("**Whille**"). Whille was required to provide monthly reports to the Supervisory Subcommittee of her activities, which she prepared from February through September 2011. Each report consists of a single paragraph concluding, "We have not identified any issues . . . ." Whille only looked at Corzine's trading to ensure that he was not

engaging in insider trading or market manipulation; this oversight mechanism was not designed with the purpose of reviewing the economic rationale of Corzine's trading decisions.

With minimal oversight of his trading activities, Corzine remained a driving force behind the Company's expanding Euro RTM portfolio. Corzine communicated with MFGI and MFG UK personnel directly regarding those trades, personally instructing them when to enter and exit various positions. Notably, to the extent anyone actively tried to oversee his trading activities for any purpose, Corzine remained one day ahead of anyone in the United States. U.S. traders and Operations Department personnel first learned about Corzine's trades the day after they were entered by MFG UK traders in London.

D. RTM Structure and Accounting

1. RTM Structure

A repurchase to maturity trade ("**RTM**") utilizes a repurchase agreement ("**repo**"), which is a sale of securities coupled with an agreement to repurchase the same securities at a higher price at a later date. Repos generally are used by financial institutions to secure short-term funding and increase leverage.

In a repo transaction, the seller transfers a percentage of the fair market value of the underlying security and assumes the obligation to repurchase the security at a later date. The difference between the fair market value of the underlying security and the repo financing amount is known as the Initial Margin or "haircut." This amount protects the repo lender against credit risk. In addition, Variation Margin protects a repo lender from a decrease in the value of the assets prior to their resale or illiquidity of the assets.

The Initial Margin level varies, depending upon the credit rating of the seller. The counterparty to a repo usually has the right to demand Variation Margin (in other words, make a

"margin call") during the term of the agreement to maintain the value of the collateral when the value of the underlying assets falls. The counterparty also may require a seller to post additional Initial Margin under certain circumstances when the seller's creditworthiness is in doubt.

2. Role of a Clearinghouse

A clearinghouse is a financial institution that provides clearing and settlement services for financial transactions. A clearinghouse may also stand between the two or more participants in an RTM transaction in order to reduce the risk for one of the parties and to reduce settlement risks by netting offsetting transactions between multiple counterparties, requiring margin deposits, providing independent valuation of trades and collateral, monitoring the credit quality of the parties, and providing a guarantee fund to cover any losses that exceed a defaulting party's collateral on deposit.

Clearinghouses can demand Initial or Variation Margin, which can create liquidity risks by requiring a clearing member to post cash and sell securities to cover its obligations.

3. RTM Accounting

It is common for a repo to either have a set term, which expires on a date that is earlier than the maturity date of the underlying security, or to be an "open" term repo, which does not have a set term and therefore "rolls" each day unless either party decides to end the arrangement. If the termination date is the same as the maturity date of the underlying security, the transaction is a repo to maturity, or RTM. While a typical repo is accounted for on a balance sheet as a collateralized financing (thus, increasing balance sheet leverage), an RTM is accounted for as a sale of the assets, and is "derecognized," or removed from the Company's balance sheet.

Unlike a traditional repo, in an RTM transaction, the counterparty keeps the pledged securities as collateral until they mature. At maturity, the counterparty may either return the

securities to the borrowing company or redeem them with their issuer at par value. In an RTM, under the Financial Accounting Standards Board ("**FASB**") standards, the borrowing company is viewed as having surrendered effective control of the securities when it transfers them as collateral to the counterparty. FASB accounting standards therefore require that the borrowing company account for the transaction as a "sale" of the securities coupled with a forward repurchase commitment (to repurchase the collateral at maturity), rather than a secured borrowing. The forward repurchase commitment must be accounted for as a derivative at fair market value on the company's balance sheet, with changes in value recognized concurrently as income or loss.

MF Global entered into Euro RTMs in order to finance the purchase of sovereign debt. MF Global would first, through MFG UK, identify and purchase the debt. Simultaneous with the purchase, the Company would sell the debt back to the clearinghouse through the RTM to offset its payment obligation. The RTM sale would finance the entire purchase of the debt minus Initial Margin, which MFG UK would be required to post with the clearinghouse. MF Global also derecognized the Euro RTMs from the Company's balance sheet and recognized the gain on the sale of those securities as of the trade date of each transaction. As discussed above, transactions were treated as a sale of financial assets with a forward purchase commitment. This allowed MF Global to immediately recognize the gain from the transaction, while simultaneously removing it from the Company's balance sheet.

E. MF Global's Investment in European Sovereign Debt

1. MF Global's Execution of Euro RTMs

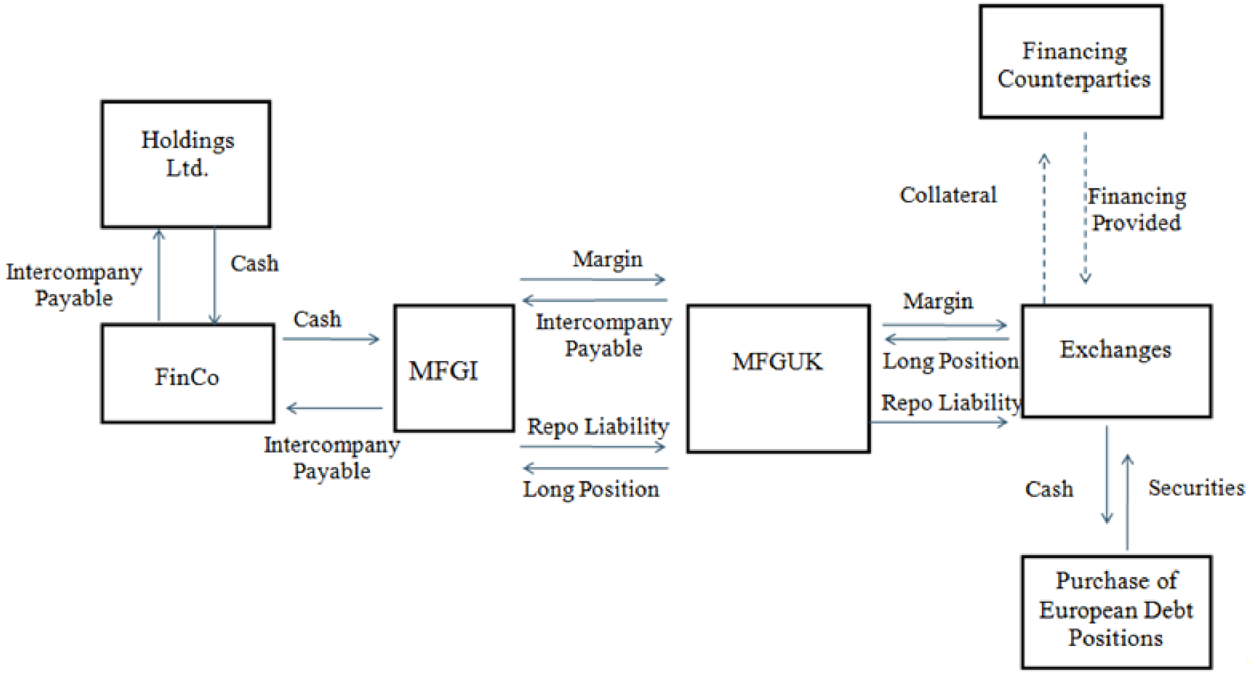
MF Global's Euro RTMs were governed by a global master repurchase agreement (the "**GMRA**"), between MFG UK and MFGI, dated July 19, 2004, and as amended. MFG UK

entered into the trades because it, and not MFGI, was a member of the relevant clearinghouses, LCH.Clearnet London and LCH.Clearnet Paris (collectively "**LCH**"), and Eurex Exchange ("**Eurex**").

To finance MF Global's Euro RTMs, MFG UK would enter into back-to-back repo transactions consisting of two legs: (1) a repo leg with third parties to finance the acquisition, and (2) a reverse repo leg with MFGI to finance MFGI's long position. By entering into the two offsetting back-to-back repos, MFG UK was "flat" to the market and did not bear any of the associated risk that may have resulted from fluctuations in the market value of the Euro RTMs. MFG UK, however, remained dependent upon MFGI to forward the funds MFG UK needed to meet its margin calls from the clearinghouses. MFG UK was not in a position to meet significant margin calls without MFGI providing the collateral to MFG UK under the corresponding repo.

The maturity of the securities underlying the Euro RTMs matched the maturity of the financing provided under MFG UK's repos with the clearinghouses, with one difference. Due to operational restrictions, clearinghouses in the United Kingdom often required the repo seller in an RTM to repurchase the underlying collateral a few days prior to the collateral's stated maturity date. In the case of MFGI's Euro RTM trades, the underlying securities had to be repurchased two business days prior to the securities' maturity date. Thus, MFGI would need to finance the positions on its own for two business days. The two-day period is referred to as the "roll-off period".

The below diagram illustrates the end-to-end structure of the Euro RTM transactions:



On the dates MFGI entered into the various Euro RTMs, it recognized a gain in the amount of the difference or spread between (1) the effective interest rate received by MF Global on the debt securities and (2) the repurchase rate (or the financing rate) paid by MF Global to the counterparty. MFG UK recognized a gain in the amount of the markup for its role as counterparty to both MFGI and the clearinghouses. The trades were held by MFGI so that it, rather than MFG UK, bore the risk of default or restructuring of the sovereign debt.

On July 1, 2010, MFGI and MFG UK entered into an investment management agreement related to the Euro RTM trades, which provided that MFG UK would identify market opportunities related to the sovereign debt of certain European governments. Pursuant to this agreement, MFG UK received 80% of the consolidated net revenue of such transactions, while

MFGI received 20% of the revenue, held the trades, and took the risk that the sovereigns would default or restructure their debt.

2. Initial and Variation Margin

As discussed above, the Euro RTMs required the payment of Initial and Variation Margin to the clearinghouses. The clearinghouses regularly changed margin requirements based on market events. Once MFG UK entered into the Euro RTM trades, the Company faced the risk that the clearinghouses would demand additional margin. Additional margin could be demanded in numerous situations: (1) increased Initial Margin could be required by the clearinghouses if they determined that the Company had become less creditworthy; (2) increased Initial Margin could also be required by the clearinghouses if the clearinghouses determined that the risk inherent in the underlying security had increased; and (3) Variation Margin could be required based on the decline in market value of the underlying security. Accordingly, financing the acquisition of securities through the use of repos had the potential to create a significant liquidity risk for MFGI and the Company as a whole.

At the time MF Global began entering into the Euro RTMs, each of the sovereign debt issuances was rated as investment grade (*i.e.*, Moody's rated "A" or higher). MFG UK, therefore, was required by the clearinghouses or third parties acting as counterparties to the trades to post only a small Initial Margin payment, in some cases as little as five percent of the face amount of the securities to be financed through the RTM. In turn, MFG UK required only this amount from MFGI, allowing the Company, through MFGI, to build a highly leveraged portfolio, without having to pledge significant capital. MFGI met its Initial Margin obligations

to MFG UK, and subsequent Variation Margin calls as required by MFG UK, using liquidity at MFGI as well as intercompany loans provided by FinCo and Holdings Ltd.

As discussed in greater detail below, once the value of the Euro RTMs deteriorated in the summer and fall of 2011, MFG UK, and consequently MFGI and FinCo, were required to post additional Variation Margin. In late October 2011, after the Company's credit rating was downgraded, the clearinghouses also required additional Initial Margin. MFG UK, as counterparty, was responsible for meeting the clearinghouse's margin calls, which at certain points were issued on a daily and intraday basis. MFG UK would then issue margin calls to MFGI, which may have funded the margin calls in whole or in part by loans from FinCo.

3. Revenues Generated by the Euro RTMs

An analysis of the Company's net loss and income over the relevant time period indicates that the Company relied heavily on the Euro RTM income to report improved earnings. For example, for the quarter ending March 31, 2011, the Euro RTM income allowed the Company to cut its net loss from approximately $92 million to approximately $46 million. For the quarter ending December 31, 2010, the Euro RTM income allowed the Company to cut its net loss from approximately $29 million to approximately $5 million. Finally, for the quarter ended September 30, 2010, the Euro RTM income cut the Company's net loss from approximately $54 million to approximately $39 million. The Euro RTM income also allowed the Company to report net income for the quarter ending June 30, 2011 of $13 million. Without this income, the Company would have had a net loss of more than $23 million.

The strategy of meeting earnings targets by relying on the Euro RTM revenues was inherently unsustainable over the long term because each new revenue-producing position

required the posting of Initial Margin, which decreased available liquidity for the duration of the investment. The liquidity demands and risks of the Euro RTM portfolio were exacerbated when Corzine lengthened the maturities of the investments, thereby further decreasing available liquidity for a longer period of time.

Additionally, despite repeated requests for risk limit increases (discussed below), Corzine exceeded the Board-approved limits for European sovereign investments on a number of occasions, including the following:

(1) On October 1, 2010, shortly after the Board's approval of limit increases at the September 22, 2010 meeting of the Executive Committee, the Company breached the Irish and Spanish limits. The Irish breach amounted to $79 million, or 16% of the country limit;

(2) At the end of November 2010, the Company breached the Italian limit by $50 million;

(3) On March 31, 2011, the Company breached the overall European portfolio limit by $184 million; and

(4) In April and May of 2011, the Company breached the Italian limit by about $400 million, and the Spanish limit by approximately $200 million.

During several fiscal quarters between 2010 and 2011, Corzine placed Euro RTM trades at or near the end of the quarter in order to generate revenue and immediate earnings for that quarter, giving a skewed picture of the Company's financial health. For example, in the last four days of the quarter ending March 31, 2011, Corzine placed Euro RTM trades worth approximately $2.62 billion. On the last day of that fiscal quarter, March 31, 2011, the Company executed several large Euro RTM trades worth approximately $1.03 billion in order to enable the Company to meet its projected revenue numbers for the quarter.

4. Corzine's Execution of Euro RTMs

Corzine was personally involved in the direction and execution of specific Euro RTMs. Before initiating a Euro RTM trade, Corzine typically would discuss the profit potential of the trade and the state of the European markets with Cantor, one of the Company's proprietary traders. On a daily basis, Corzine received information from the MFG UK fixed income traders on opportunities in the European bond market, including a daily matrix showing potential profits for certain European sovereign positions. Corzine communicated directly, or through Cantor, with trading desk personnel in New York and London, instructing the trading desks when to enter and exit various positions.

Corzine himself acknowledged that the Euro RTM positions were his "personal responsibility" and "a prime focus" of his attention. Moreover, speaking to investors in May 2010, Corzine plainly stated the bounds within which he intended to conduct the trading:

> It's not risk systems that will determine whether we have losses. It will be **mistaken judgments in the first instance that go beyond limits which I don't intend to allow to happen. . . . But the goal here is not to be a prop trader.** And if we change that view, we'll speak to it directly. But we're of the view that I think the greatest risk is that it undermines revenues in a given quarter or given time frame but **I don't think that we will be in a risk taking position, substantial enough to have it be the kind of thing that rating agencies would say, holy cow, these guys have got a different business strategy than what we told them we had**.

(Emphasis added.)

5. Initial Increases to European Sovereign Risk Limits

When Corzine joined MF Global in March 2010, the Company held approximately $400 million in the sovereign bonds of the IPSI countries. These positions were financed through traditional repos. Risk limits for investment in this debt were set under the Company's

Delegations of Authority ("**Delegations**"), which provided a structure for granting authority to management for approving levels of expenditures, entering contractual obligations, and transacting other significant business for the Company. As a result of the Greek economic crisis, which started in March 2010, the Risk Department revised the Delegations, setting specific limits around investments in each country.

In June 2010, the Fixed Income and Treasury Departments in the United Kingdom sought a $1 billion aggregate limit for all sovereign debt. The CRO at that time, Roseman, had the authority to approve, and did approve, this request under the Delegations. Roseman did not believe that there were significant risks with a $1 billion limit, although at the time he was more concerned than Corzine about the potential default risks associated with the European sovereigns. In Roseman's view, the liquidity risks of the positions were not material at this point because of the size of the limits and the Company's ability to fund or liquidate the positions if conditions changed.

Corzine and the traders continued to request increases in the European sovereign limits. As the European sovereign positions and limits approached $1.5 to $2 billion in mid-September 2010, Roseman became increasingly concerned about the associated liquidity risks and capital risks relative to the Company's approved risk appetite. Roseman also believed that the capital risks associated with the positions were becoming material and could expose the Company to the potential loss of $100 to $200 million in margin calls. Under the Delegations, Roseman had the authority to approve increases up to $2 billion, but felt that a request to increase the limits to that level, which required specific country limits to be set and approved by the Board, should be

presented to the Board. Roseman expressed these concerns to Corzine in or about late August or early September 2010, and the two agreed to consult the Board at its mid-September meeting.

6. Corzine Asks the Board to Increase the Risk Limit to $4.5 Billion

The CRO first updated the Board regarding the Company's Euro RTMs at a meeting held on August 12, 2010, although no limit increases were sought at that time. At the September 22, 2010 meeting of the Board's Executive Committee, Corzine requested that the European sovereign limits be increased to $4.5 billion.

The Executive Committee was comprised of the four Directors who chaired the various Board committees: Corzine, Fusco, Gelber and Goldberg. The Executive Committee approved the increase to $4.5 billion, and the full Board ratified the Executive Committee's decision at its next meeting on October 28, 2010.

In approving the increase to $4.5 billion, the Executive Committee also set individual country limits for Spain ($2 billion), Italy ($1.5 billion), Ireland ($500 million), and Portugal ($500 million). As of September 30, 2010, just a week after the vote, the Company already had breached the new limits set for Ireland and Portugal, holding $586 million in Irish debt and $503 million in Portuguese debt.

In October 2010, MF Global's European sovereign portfolio rapidly approached the $4.5 billion overall limit set by the Executive Committee in the prior month. At this time, Roseman met with Corzine to express concerns about the liquidity and capital risks of the Euro RTM trades.

7. Corzine's Growing Bet

Corzine continued to initiate requests for limit increases in the Euro RTM portfolio, and made presentations to the Board on the portfolio in connection with risk limit increases. Corzine

apparently convinced the Board that there were opportunities for the Company to increase its profits by making large scale investments in certain countries.

Significant time was spent during Board meetings and meetings of the Board's various committees discussing and debating both the Company's positions and the attendant risks associated with those positions. Most members of the Board were present for these discussions, as the Board had a policy that any member of the Board could attend any meeting of any Board committee, even if the individual Board member was not officially a member of that committee.

Corzine spent time during each of these presentations telling the Board that there were no default risks associated with the Euro RTMs, because, among other reasons, the European zone, with the exception of Greece, was protected by the European Financial Stability Facility ("**EFSF**"). The EFSF was a special purpose vehicle financed by members of the Eurozone countries which have adopted the Euro. It was created to safeguard financial stability in Europe by providing financial assistance to Eurozone states.[12] Corzine also stressed that the risk of default was further minimized because MFGI held positions with varying maturities.

Corzine consistently represented to the Board that the Company's investment in Euro RTMs was a "bridge" in the Company's revenue stream as the Company transitioned from making money on interest rates and commissions to becoming a B/D and investment bank. He believed it was a temporary opportunity in the market to obtain revenues during the Company's

[12] Corzine relied heavily on the existence of the £440 billion EFSF, established in May 2010 and scheduled to expire in June 2013. However, while the EFSF may have insured against some risk of issuer default, it is not clear how much protection EFSF funds afforded the Company from exposure to the European market. Even if funds were made available to a sovereign, the sovereign elected how to use the funds and which bondholders to pay. It is also not clear that EFSF funds could cover multiple countries defaulting at once. Thus, if the EFSF did not completely cover defaulting debt securities or if the securities were restructured, MFGI would not be paid in full at their maturity, even though MFGI would still have the obligation to buy back the debt from the counterparty in full at par value.

transformation. The "bridge" metaphor illustrates the temporary nature of the strategy and opportunity, as European countries were not going to offer such yields on their bonds indeterminately. One MF Global officer characterized the Euro RTMs as a "band-aid," rather than a business model.

At a meeting of the Audit and Risk Committee held on October 27, 2010, Roseman also discussed the Company's exposure to Irish sovereign debt, and the attendant market and stress risks associated with the positions. At the time, the Company's capability to model market risk was not fully developed.

a. Corzine Seeks Risk Limit Increase to $4.75 Billion

On November 8, 2010, less than two months after the initial European risk limit increase request, Corzine requested an additional increase in the risk limit to $4.75 billion, explaining that there were opportunities available in making incrementally larger investments in investment-grade countries. After discussing the accounting treatment, risk scenarios, liquidity risk, and stress testing, the Board approved Corzine's request. The Board approved increased limits on individual country exposures for Spain ($2.5 billion), Italy ($1.75 billion), Ireland ($1 billion), and Portugal ($900 million). The Board also restricted additional purchases of Irish and Portuguese debt.

At the meeting, Roseman informed the Board that the positions exposed MF Global to potential margin calls of $524 million under one of four liquidity stress scenarios. Roseman based this figure on a 15% haircut applied across all sovereigns because, at the time of this meeting, LCH had raised the haircut associated with the Irish positions from 7% to 15%. Roseman told the Board that at $4.75 billion, the positions were material but manageable.

Several Board members, including Fusco and Schamis, challenged Roseman's assumptions underlying the across-the-board 15% haircut. The Board struggled to understand this measure because, in the Board members' view, such a haircut ignored the distinct economic profiles of the different countries in the portfolio. The Board questioned the assumption that the correlated liquidity risk scenarios could materialize across all counterparties and issuers at the same time. In order to better understand Roseman's position, the Board requested that he provide a written analysis of his position.

On November 29, 2010, Roseman provided a memorandum to the Board with the requested analysis. The memorandum described incremental liquidity stress funding needs of $524,409,330. Between the time the Board approved the risk limit increase on November 8, 2010 and the time Roseman distributed his written risk scenario assessment on November 29, 2010, LCH had requested an additional 15% haircut on Irish positions, for a total of 30%. Subsequently, the Company moved these Irish positions to Eurex, a different clearinghouse, in order to benefit from a lower haircut of 6.05%.

b. The Board Temporarily Halts European Sovereign Debt Trading Between December 2010 and January 2011

The Board again discussed the Euro RTM portfolio and associated stress testing at its December 15, 2010 meeting. The discussion included worst-case scenarios in the event of sovereign default and the risk profiles associated with certain sovereigns. As reflected in the minutes of the meeting, the Board decided not to increase the risk limits for European sovereign trading, and instead requested the ability to continue to review the portfolio at its regularly scheduled meetings. The Board further agreed that the Company "could continue to hold, roll

forward (prior to a roll-off or otherwise) and re-finance the current [s]overeign positions in its portfolio, all within the limits under the risk [Delegations]."

At either the November or December 2010 Board meeting, Corzine and Roseman disagreed about whether Roseman's worst-case liquidity stress scenario was realistic. Steenkamp, Abelow and MacDonald also were present at the November and December 2010 Board meetings. During each of these meetings, the Board received assurances from management that the Company had sufficient liquidity resources from its revolving credit facilities ("**RCF**") and other credit lines to manage even Roseman's worst-case scenario. MF Global relied on two separate RCFs for short-term liquidity needs: (1) a $1.2 billion unsecured committed revolving credit facility for which Holdings Ltd. and FinCo were the borrowers; and (2) a $300 million secured committed revolving credit facility for which MFGI was the borrower and Holdings Ltd. and FinCo were guarantors.

During this period, the Company began investing in longer-dated Euro RTMs. Trades entered during the September 2010 time period ranged from six to twelve months. Beginning in December 2010, the maturity dates were lengthened from anywhere between nine and twenty-one months. At the same time that the maturities began to lengthen, even doubling, the amount of these transactions also increased, creating an additional burden on the Company's capital and liquidity resources.

At a meeting of the Audit and Risk Committee held on January 27, 2011, the Board and management agreed that the Euro RTM portfolio should wind down, meaning positions should be allowed to roll-off and that no additional positions should be placed, unless Corzine requested that the Board grant him authority to enter additional positions. At least one Board member,

Gelber, recalled that the Board's decision to halt the growth of the investments was due to concerns about the size of the positions and the volatile economic situation in Europe.

c. Corzine Hires Stockman to Replace Roseman

In September 2010, Corzine retained a search firm to find a new CRO for the Company. Roseman had begun to lose management's confidence much earlier, during Dan's tenure as CEO. Dan had expressed his and then-CFO MacDonald's frustration with Roseman to the Board as early as August 2009. Roseman also submitted to a coaching and assessment process that Dan perceived as unsuccessful. In January 2010, management decided to replace Roseman.

However, upon Corzine's arrival, the search for Roseman's replacement was put on hold pending Corzine's review of the Company's business. The Company did not begin in earnest to conduct a search for a new CRO until September 2010.

In November 2010, Corzine informed Roseman that the CRO would no longer report directly to the CEO, Corzine, but would report instead to the COO, Abelow. Roseman disagreed with the change in the CRO's reporting line because he felt it demoted his position and disempowered the Risk Department. Roseman expressed his objections to Corzine and Fusco, the chair of the Audit and Risk Committee.

At the end of January 2011, Roseman was notified that he was being replaced by Stockman, effective immediately. Corzine testified before the House Committee on Agriculture on December 8, 2011 that he felt the Company needed someone "more fully attuned to the broker-dealer side of [the] business" as its CRO.

d. Corzine Seeks Risk Limit Increase to $5 Billion

Even with management's assurances, some Board members grew increasingly concerned about the size of the Euro RTM portfolio. In a February 24-25, 2011 email exchange between Stockman and Glynn, Glynn stated:

> One of my risk concerns is the level of European sovereign subprime exposure and the consequences to the [Company] if haircuts are applied as a result of restructurings, downgrades, liquidity events, counter party issues, collateral calls etc. You will be under tremendous pressure at the [Company] to approve higher risk limits in non core areas to support earnings weaknesses elsewhere.

Despite Glynn's concerns, for the first several months of his tenure, Stockman believed that the risk profile associated with the Euro RTMs was acceptable in light of then-prevailing market conditions. His views also were based partly on information received from executives in the Finance Department that the Company possessed adequate sources of liquidity to address its needs even under stressed market conditions.

In the middle of February 2011, approximately a month after Stockman joined the Company, Corzine asked Stockman to prepare a formal Board request to increase the global sovereign limit from $4.75 to $5 billion. Corzine initially had considered requesting a much higher limit increase.

In preparation for the Board meeting on March 2, 2011, during which this request was to be delivered, Stockman asked two executives in the Risk Department to prepare a Board memorandum approving the increases while explaining the risks. The two executives were Talha Chaudhry ("**Chaudhry**"), CRO for the Americas and Global Head of Market Risk, and Stephen Hood ("**Hood**"), Head of Market Risk, Americas. At the time, Stockman was still

familiarizing himself with the Company's business, yet his explicit instruction to Chaudhry and Hood was to draft a memorandum supportive of Corzine's new limit increases.

Stockman's memorandum to the Board ultimately supported Corzine's request for an increase in the overall limit from $4.75 to $5 billion, with a temporary increase to $5.8 billion until March 31, 2011, at which time the limit would return to $5 billion. The purpose of the temporary increase was to facilitate replacement trading during the roll-off period. Stockman also supported increases in individual country sovereign debt limits for Italy (from $1.5 billion to $1.8 billion), Portugal (from $1 billion to $1.3 billion), and Spain (from $1.75 billion to $2.3 billion), a reduction for Ireland (from $1 billion to $0.75 billion), and a new limit for Belgium ($500 million).

Stockman conditioned his support for these increases on confirmation from the Finance and Treasury Departments that the Company would have the liquidity necessary to fund these positions, even under volatile conditions, for both the $5 billion and temporary $5.8 billion portfolio limits. Ultimately, Stockman was convinced that the liquidity scenarios and the associated margin calls were acceptable based on assurances that the Company had sufficient liquidity to cover the maximum requirements predicted under the Risk Department's stress scenarios.

At the time of the March 2 meeting, MacDonald still formally held the title of CFO, although he had been appointed Head of Retail as of December 15, 2010, and he had turned his attention to that job as early as the summer of 2010. Steenkamp, while performing in the role of CAO, had been identified as MacDonald's replacement. Steenkamp routinely attended Board meetings before and after being formerly appointed CFO in April 2011.

The memorandum Stockman presented to the Board during the March 2 meeting outlined the liquidity risks associated with the Euro RTM portfolio by setting forth potential liquidity needs under two risk scenarios. Scenario 1 in the memorandum stated: "(*Plausible*): The yields on Ireland and Portugal widen by 200 bp while Spain and Italy widen by 50 bp. As a result, the haircuts increase from their base case by 30% for Ireland, 15% for Portugal and stay the same for Spain and Italy." Under Scenario 1, Stockman projected potential funding needs for the Euro RTM portfolio of $297 million. Scenario 2 stated: "(*Less Likely but not impossible*): The yields on Ireland widen by 500 bp, Portugal by 350 bp, Spain by 250 bp and Italy by 150 bp. As a result, the haircuts increase from their base case by 45% for Ireland, 15% for Portugal, 15% for Spain and 5% for Italy." Under Scenario 2, Stockman projected potential funding needs for the Euro RTM portfolio of $761 million. He concluded that an approximate 15% increase to the projected margin needs outlined under the two risk scenarios had to be applied to account for the temporary growth of the portfolio to $5.8 billion until March 31, 2011. Stockman's funding risk analysis assumed that the exchanges, clearinghouses and counterparties would continue to accept sovereign debt as collateral. The total amount of margin posted for the portfolio at the time was approximately $105 million.

After the presentation on March 2, 2011, the Board approved the requested permanent and temporary limit increases ($5 billion and $5.8 billion, respectively), but stipulated that management would need to seek advance approval from the Board or the Executive Committee if it sought to exceed the limits or significantly add to the positions beyond the existing roll-off periods.

e. Corzine Seeks Additional Risk Limit Increases in March 2011

On March 23, 2011, Corzine approached the Executive Committee for an extension of the temporary increase in the overall limit approved less than three weeks earlier. Corzine sought to extend the temporary increase of $5.8 billion through September 30, 2011, and to revise certain individual sovereign debt limits within the Euro RTM portfolio. He explained that the currency appreciation of the Euro accounted for approximately one-half of the limit increase request.

Stockman and his staff in the Risk Department had spent three weeks analyzing the Euro RTM trades and associated issues in preparation for the March 2, 2011 Board meeting. In light of the efforts made to prepare for that risk increase, it was unclear to Stockman why this new request was coming so quickly on the heels of the last request. In a March 18, 2011 email exchange with Abelow, Stockman expressed his discomfort at the frequency of the limit increase requests:

> I should expect to hear a request to go to circa $6bn after March 31, in addition to new country mix (increase [I]taly, reduce [S]pain and [I]reland, slight inc to [P]ortugal). Doubt he has called board. Keep me posted on anything u hear. I will do same. Stating the obvious, we just finished review suggest[ing] 5bn was our appetite . . . .

Despite his reservations, Stockman supported the March 23, 2011 request, citing the diversification of the portfolio, risk reductions achieved through investments in higher credit-grade sovereigns such as Italy, and decreased investments in lower credit grade sovereigns such as Ireland and Portugal.

The majority of the Executive Committee also approved the request to extend the temporary $5.8 billion limit until September 30, 2011, at which time the limit would revert to $5

billion, provided that the maturity dates for the bonds underlying the Euro RTMs did not extend past December 2012. The Executive Committee modified the individual country limits for Italy (increased from $1.8 to $3.1 billion), Spain (reduced from $2.3 to $1.5 billion), Ireland (reduced from $750 million to $400 million), and left Portugal unchanged ($1.3 billion).

The Executive Committee granted the increase in the Italian limit (from $1.8 to $3.1 billion) to allow Corzine to take advantage of opportunities in the market. In March 2011, Corzine placed $2.94 billion worth of Italian bond trades. The increased trading in Italian bonds caused MFGI to become concentrated in a single Italian bond issuance with a maturity date of December 31, 2012, and eventually attracted the attention of the Financial Services Authority ("**FSA**"), the body responsible for regulation of the financial services industry in the United Kingdom.

Fusco voted against Corzine's request to extend the temporary $5.8 billion increase through the end of September. She supported an increase in the portfolio only to the extent necessary to account for possible currency appreciation.

A week after this request, on March 31, 2011, Corzine sought yet another increase in the individual country limit for Belgium from $500 million to $1 billion. The Executive Committee approved this request.

f. Stockman Warns of Possible Increased Margin Requirements

At a May 11, 2011 meeting of the Board, Stockman provided an update on the Euro RTM portfolio, market events, volatility, probability of sovereign default, and results of stress testing performed by the Risk Department in connection with the Euro RTM portfolio. Stockman's presentation highlighted the risk of increased margin requirements and the liquidity drain on MF

Global's overall business, as well as the uncertainty and volatility in the market surrounding these positions. Corzine did not seek additional increases in the Euro RTM limits at this meeting.

Stockman also explained to the Board that the total funding needs between March 1 and May 5, 2011 amounted to $167 million, and that, in the same period, there were spread movements of greater than 300 basis points for Portugal and greater than 125 basis points for Ireland.

At this point, Corzine and Steenkamp recognized the potential for the clearinghouses to make demands for additional margin that could significantly impact the Company's liquidity. Stockman informed the Board that, as a result of the volatility discussed above in connection with Portuguese and Irish debt, LCH had increased the haircut or Initial Margin for Portugal from 0% to 45%. The increased margin demand had the potential to create an additional $500 million funding requirement, but MF Global had managed to enter into offsetting positions with LCH while concurrently moving the risk to Eurex to reduce margin requirements until September 2011. As a result, funding needs on the portfolio had only increased from $105 to $167 million, instead of by an additional $500 million.

Stockman also told the Board that the Company was using more of its limits for the IPSI nations due to the placement of new positions, weakening of the dollar against the Euro, and increases in the maturities of the IPSI holdings. As a result, the stress scenario analysis conducted by the Risk Department showed increased funding projections for the portfolio since March 1, 2011. Under one stress scenario, the liquidity needs were projected to increase from $297 million to $331 million.

g. Corzine Seeks Additional Risk Limit Increases in June 2011

Despite Stockman's presentation in May 2011 highlighting the portfolio's growing funding needs, just one month later Corzine sought an additional increase in the permanent European sovereign debt limit from $6.8 billion to $8.5 billion. On June 6, 2011, Corzine called an off-cycle meeting of the Board, held via telephone, in order to present the request and to take advantage of an immediate market opportunity.

During the June 6 meeting, Corzine advised the Board of the positive potential returns on investment and how the request fit within the Company's strategy, which he described as including taking thoughtful, measured risk. Corzine also recommended that the Euro RTM portfolio be remodeled into tiers, with Tier 1 encompassing Belgium, Spain, and Italy; Tier 2 encompassing Ireland and Portugal; and Tier 3 encompassing Greece. The purpose of organizing the portfolio into tiers was to consider separately additional investments in higher quality, less risky sovereigns, for which there was more liquidity, and investments in lower quality sovereign bonds, for which there was less liquidity and higher spreads. Corzine requested a $700 million increase for Tier 1 and a $300 million increase for Tier 2.

Stockman provided the Board with a memorandum supporting Corzine's request. He indicated that the Company's existing positions required liquidity of approximately $200 million with an anticipated additional $50 million associated with the requested increase. Under the two different stress scenarios developed by the Risk Department, potential funding requirements were increasing substantially as a result of the proposed limits: Scenario 1, from $331 million to $500 million; Scenario 2, from $664 million to $1 billion.[13]

[13] These risk scenarios were based on the same assumptions as the scenarios Stockman presented to the Board on March 2, 2011.

Stockman's analysis also suggested that active management and hedging of the portfolio might be needed, particularly for Italy and Spain, but he also noted that these hedges may not achieve the expected liquidity risk offsets.

Scenario 2 would have required liquidity very near the limit of the Company's unsecured RCF of $1.2 billion, although this was not the intended use of these funds. As Corzine told investors in February 2011, the RCFs were intended to serve as a backstop for extraordinary situations, "a liquidity pool and not a component of [the Company's] long-term capital structure."

Steenkamp, in his capacity as CFO, responded to the Board's questions regarding the Company's liquidity position in case of certain default scenarios. Steenkamp told the Board that the Company would have the ability to fund even the most severe stress scenario presented by Stockman. Steenkamp assured the Board that the Company had adequate sources of liquidity to finance the increasing positions under severe stress conditions. In support of his view, Steenkamp cited MF Global's $1.2 billion RCF, sellable securities, and the capital raised by the Company through recent debt issuances. Steenkamp believed that the Company's $1.2 billion RCF was a significant buffer to support the Company in case of emergency liquidity needs.

The Board approved the increase in the Tier 1 limit by $1 billion – more than the $700 million requested by Corzine – but approved only a $200 million increase for Tier 2 – less than the $300 million requested by Corzine. The Board also approved a $200 million increase for Ireland, but did not approve any risk limit increase for the Portugal portfolio, keeping the limit at $1.3 billion. The Board also imposed a maturity date limit of June 30, 2012 for the Portugal and Ireland investments and a maturity date limit for Tier 1 countries of December 31, 2012.

Thus, after the June 6 meeting, the overall limit was increased to $8.5 billion with individual country risk limits set as follows:

Tier or Individual Country	**Limit Increase**
Tier 1 (Belgium, Italy, and Spain)	From $5.6 billion to $6.6 billion
Belgium	From $1 billion to $1.5 billion
Italy	From $3.1 billion to $4 billion
Spain	From $1.5 billion to $2 billion
Tier 2 (Ireland and Portugal)	From $1.7 billion to $1.9 billion
Ireland	From $400 million to $600 million
Portugal	$1.3 billion limit remained unchanged

h. Stockman Advocates Hedging and a Halt to Trading

As market conditions worsened in early July 2011, Stockman began to express concerns to management. Stockman believed that, over the summer, the probability of default, stress scenarios and margin calls had increased significantly. As the credit market deteriorated, Stockman came to the view "that it would be prudent for the [C]ompany to mitigate the increased risks associated with its European sovereign [RTM] positions, and to consider entering into hedging transactions to reduce the [C]ompany's exposure."

To alert management to the growing risks of the Euro RTM positions, Stockman convened two meetings in July 2011 with Corzine, Abelow (who only attended the second meeting), Steenkamp and senior traders, to discuss the risks and exposures of the Euro RTMs, stress scenarios, and the possibility of hedging the positions. Stockman highlighted the financing risks associated with certain aspects of the Italian and Spanish bonds, the need to rectify multiple

breaches of the gross limits set by the Risk Department (which had accumulated to 20% over the Italian gross limit; 31% over the Spanish gross limit; and 12% over the overall Tier 1 gross limit as of July 2011), and the need to engage in additional hedging and risk reducing strategies. Stockman also presented updated information under the stress scenarios he previously presented to the Board that indicated projected funding requirements of $988 million under the less severe stress Scenario 1, and $1.6 billion under the more severe stress Scenario 2, exceeding even the available funds under the unsecured RCF.

At Stockman's first meeting with management on July 13, 2011, Corzine challenged Stockman's analysis, and ultimately disagreed with his recommendation to hedge the Company's exposure. In a summary of the meeting, Stockman explained that he recommended hedging as a means of addressing the Company's exposure to large margin calls, which remained the principal risk associated with these positions.

Stockman held a second meeting on July 21, 2011, and delivered the same message he gave during the first meeting: hedge the Company's exposure. The current funding requirements, now at $480 million, were up by approximately $200 to $300 million over the previous month. Projected funding needs increased again under the two stress scenarios Stockman had previously presented: under Scenario 1, funding needs increased to $1.1 billion; under Scenario 2, funding needs increased to $1.8 billion. Stockman also added a new Scenario 3 that isolated rollover risk, or the risk that MF Global would not be able to fund the roll-off period. Stockman's rollover risk analysis indicated that if the reverses could not be rolled over, the Initial Margin would increase from $248 million on each roll date to a peak of $860 million on September 28, 2011. Scenario 3 assumed that there were no other changes or movements in

margin, positions, or market prices during this period, and warned that any other adverse scenario would have an incremental impact on the numbers presented in Scenario 3.

Despite his warnings, Stockman did not observe any meaningful hedging after these meetings or any new steps to address the substantial risks presented by the Euro RTM portfolio. Management did not support hedging of the portfolio, even though Corzine easily could have directed the traders to begin hedging the positions. An analysis of the Company's Euro RTM portfolio reveals that no significant hedging in the form of short positions was entered into until a French netting trade was entered in or about September 2011.

On July 29, 2011, Corzine purchased another $200 million of Italian bonds. Although the purchase was within Board-approved limits, the exposure was not hedged by any offsetting trades.

On the following day, July 30, 2011, Stockman sent an email to Corzine and Abelow addressing the additional Italian bond purchases and stating that he thought the Company needed to balance the trading activity risks with the "ability to generate intelligent risk adjusted revenues, maintain our ratings, execute our plans and build our businesses." Stockman stated: "**I am not currently supportive of buying more sovereigns**." (Emphasis added.) At this time, Stockman's updated projections showed potential incremental liquidity needs of $250 million and $1 billion in addition to the $600 million margin already posted by the Company.

In the days after this email exchange, Stockman again expressed his frustration with the Italian bond purchases to members of management and explained once more that he thought it was time to limit exposure in the Euro RTM portfolio. Stockman did not receive any indication that management supported his recommendations.

i. The Board Halts Trading

The Board had debated the impact of the Euro RTM positions and the wisdom of Corzine's strategy repeatedly from the fall of 2010, with individual Board members having varying levels of comfort with the size of the trades, the benefits of Corzine's trading strategy, and the corresponding impact of the trades on the overall liquidity of the Company. As the Euro RTM portfolio expanded in 2011, Board members who were initially comfortable with the positions became less comfortable. The Board became increasingly concerned over the size of the Euro RTM portfolio, Corzine's repeated requests for risk limit increases, the concentration of the portfolio in a small number of countries, and the state of the European economy.

At least one Board member, Schamis, was also concerned about the accounting-driven structure of the Euro RTMs. Schamis understood that Corzine engaged in the trades because of the accounting benefits and so that the Company could recognize profit upfront and satisfy the rating agencies, but he did not like the RTM structure. He felt that by structuring the trades as RTMs rather than buying the bonds outright, the trades were less liquid and less profitable. He was concerned with the Company's ability to exit the trades if it became necessary to do so.

Corzine understood that the Board was becoming increasingly uncomfortable with the portfolio. He expressed to one Board member that, if the Board did not agree with him, then perhaps it needed someone else to run the Company. Corzine told the Board member that he was willing to step down if the Board lost confidence in him.

At an August 11, 2011 meeting, the Board finally halted any further growth of the Euro RTM portfolio and expressly precluded Corzine from entering into new positions notwithstanding the Board-approved limits. Stockman reported that the Tier 1 portfolio had

grown by $1.1 billion in Italy and $800 million in Spain, with no changes in the net Tier 2 holdings. The Euro RTM portfolio's funding requirement had dramatically increased from $170 million on May 5, 2011 to $500 million as of August 8, 2011, including a $50 million increase over the most recent two-week period. Steenkamp presented an update to the Board at the same meeting showing that MFGI had to fund Euro RTM margin calls amounting to $441 million as of July 25, 2011 ($278 million in Initial Margin and $163 million in Variation Margin), and a margin call of $14 million that day.

Stockman also provided stress Scenarios 3 and 4 to the Board on August 11. These stress scenarios were meant to supersede Scenarios 1 and 2 that Stockman had presented to the Board in the past. An updated Scenario 3 presented a potential $246 million incremental funding requirement for a total of $745 million ($505 million Initial Margin and $240 Variation Margin). This Scenario 3 considered a sovereign market that had deteriorated to a slightly worse position from where it was in July, resulting in increased Variation Margin requirements by the clearinghouses. A new Scenario 4 presented a $930 million incremental funding requirement for a total of $1.43 billion ($981 Initial Margin and $448 Variation Margin). Scenario 4 considered market movements that would result in LCH demanding additional margin for Italy and Spain, and assumed that MF Global would only be able to move half of its exposure from LCH to Eurex. The $1.43 billion funding requirement under Scenario 4 would have exceeded even the liquidity available under the Company's unsecured RCF. The total funding needed under the two scenarios more than doubled in comparison with previous scenarios.

Nevertheless, management continued to assure the Board that the Company had sufficient liquidity through its secured and unsecured RCFs and other sources to manage even the most

severe liquidity stress scenarios presented by Stockman. Corzine, Stockman, Abelow and Steenkamp all were present at the August 11, 2011 Board meeting.

The Board's decision to halt trading was a surprise to Corzine. The Board voiced the opinion that Corzine should think of alternate trading strategies to generate profits for the Company and that too much of the Company's balance sheet was dedicated to these trades.

After the August 11, 2011 meeting, Goldberg and Gelber, two Board members who had previously been among the most supportive of the Euro RTMs, told Corzine that they did not want to see any maturities extended and that the positions should naturally expire at the end of December 2012.

F. The "Break the Glass" Analysis

In the summer of 2011, several Board members, including Schamis, asked Corzine and Steenkamp to perform an analysis of the financial impact to the Company in the event of a credit rating downgrade. Schamis made the suggestion to management and other members of the Board at least in part in reaction to the problems at Lehman Brothers and AIG in 2008. Schamis saw the analysis as a good practice because the Company had been having an ongoing dialogue with U.S. regulators regarding their demands that MFGI reserve additional capital due to the Euro RTM holdings. Schamis felt that the analysis was warranted in light of the overall economic situation in the U.S. and Europe at the time. Furthermore, he believed that this kind of analysis was necessary for any company dependent on outside sources of funding for its survival.

The Board tasked Steenkamp with overseeing what came to be known after Holdings Ltd. and FinCo filed for bankruptcy as the "Break the Glass" analysis. Abelow joined Steenkamp in directing the analysis and they enlisted Brian Palmieri ("**Palmieri**"), Global Head of Financial

Risk Assurance, the Company's new Global Treasurer, Vinay Mahajan ("**Mahajan**"), Chaudhry and an analyst who worked under Mr. Palmieri. The group began meeting in the latter part of August 2011. As of August 2011, Steenkamp had not set a deadline for the analysis to be completed.

To develop the analysis, Palmieri, Mahajan, and Chaudhry reviewed and discussed the various scenarios, downgrades, economic factors, stock prices and other considerations presented in the Company's existing risk reports. They also interviewed the heads of each product desk, asking about liquidity issues each desk would face in the event of a downgrade and how their businesses would be affected from a profit and loss standpoint. Mahajan, Chaudhry and Palmieri collected the information and presented drafts to Steenkamp and Abelow, reporting their progress along the way. Although Steenkamp and Abelow had few substantive comments on the analysis, each questioned the overall conclusion that the Company would survive the downgrade scenarios presented. Their questions demonstrated that Steenkamp and Abelow understood the precariousness of the Company's financial position during this period of time. In an October 10, 2011 email to Steenkamp, Abelow stated:

> I [do not] have any real confidence at this point that we know our liquidity in each of days 1-7 in event of a stress event. This is troubling as we need to provide an answer to [the Board] and [Corzine] and I need to know so that we can assess if there are steps we need to take over [the] next several weeks.

Steenkamp responded, sharing Abelow's concern: "I felt the same way in reading through this, Brad. It felt like a good story at each milestone (day 0, day 7, day 30), but that assumes we get there."

The Break the Glass analysis did not adequately assess the operational challenges that the Company would face in a downgrade environment. The analysis incorrectly anticipated that the balance sheet would be reduced by a sale of assets through orderly processes. The analysis concluded that if the Company sold its positions in securities, it would get cash. The analysis did not consider how systems might be compromised or clogged in a downgrade environment and limit the efficiency with which the Company could operate or other factors that might impact the Company's order operations in this environment. In short, the analysis did not consider many of the events that did, in fact, take place during the last week of the Company's operations.

Abelow, who managed and oversaw the Operations Department, failed to raise the possibility that the Company might not operate normally during a significant downgrade and potential run on the bank. Although Abelow communicated that his team would need to be ready for a downgrade situation, it is unclear what he did to ensure that they would be. Mahajan, Chaudhry and Palmieri never spoke with employees in the Operations Department, relying instead on Abelow's assurances that he would manage the execution side in a wind-down scenario.

The Break the Glass analysis was previewed for certain officers and Board members in September by Stockman, Mahajan, and other employees who reported to them. The analysis was presented to the Board on or about October 19, 2011.

G. FINRA Capital Charge

1. MF Global Faces Increased Regulatory Scrutiny as a Result of the Euro RTM Portfolio

Increased regulatory scrutiny in the spring and summer of 2011 also contributed to strains on MF Global's resources and liquidity pressure. The scrutiny, not surprisingly,

focused on the ballooning Euro RTM portfolio and ultimately led to MFGI being assessed a capital charge by FINRA to accommodate the size of that portfolio.

Shortly after MFGI filed its May 2011 Financial and Operational Combined Uniform Single Report required by SEC Rule 17a-5 (the "**FOCUS Report**"), FINRA inquired about the Euro RTMs disclosed in the report. During May, June, and July 2011, management met and spoke with FINRA and worked to prepare responses to its inquiries.

2. Debate with FINRA Regarding Capital Charge

By early August 2011, FINRA clearly articulated its expectation that MFGI should take some sort of capital charge with respect to the collateral supporting the Euro RTM portfolio in order to increase the Company's reserves related to that portfolio. FINRA likened the Euro RTMs to long positions in sovereign debt (which are treated as nonconvertible debt and carry a capital charge), rather than RTMs of U.S. Treasuries (which carry no capital charge). After a call in which FINRA indicated that it would like the Company to determine a "Proposed Default Risk Charge," Matthew Hughey ("**Hughey**"), MFGI's Regulatory Capital Comptroller, prepared five scenarios identifying potential charges that could be assessed on the Company by FINRA. The proposed charges ranged from $7.6 million to $98.2 million.

On August 11, 2011, MF Global submitted a memorandum to FINRA objecting to FINRA's characterization of the Euro RTMs, but nevertheless proposing a charge of $55.8 million. However, FINRA rejected MFGI's proposed capital treatment, noting that there was no reason for accepting MFGI's position that FINRA differentiate between the bonds based on

country of issuance or credit rating for haircut purposes or impose smaller haircuts than those required under the net capital rule.

In anticipation of a FINRA charge, FinCo loaned MFGI $60 million on a subordinated basis, increasing MFGI's excess capital to $135 million. The Company also began discussing options to transfer the Euro RTMs to FinCo, MFG UK or a third party, but none of the options considered was viable. The transfers would have resulted in the recognition of immediate losses, the posting of additional capital, or significant regulatory opposition.

On or about August 15, 2011, Corzine and other MFGI executives met with the United States Securities and Exchange Commission ("**SEC**") in Washington, D.C. to challenge FINRA's interpretation of SEC Rule 15c3-1. After the meeting, FINRA informed MFGI that it would not change its position.

In a subsequent phone call, the SEC's Associate Director in the Division of Trading and Markets informed MFGI that there would be no further appeal, and that MFGI had to comply with FINRA's capital treatment directive. The SEC later stated that, at a minimum, MFGI should have asked the agency about the regulatory net capital treatment of the European bonds before entering into the Euro RTMs.

On August 24, 2011, FINRA imposed a $255 million capital charge on MFGI, requiring the Company to take a charge on all Euro RTMs. Although the Company objected to the charge, it took steps to avoid being out of compliance for the August FOCUS Report by increasing excess funds by an additional $183 million.

3. Consequences of Re-Filing the July 2011 FOCUS Report

On August 29, 2011, FINRA and the SEC also notified MFGI that the new capital charge applied retroactively, requiring the Company to restate its July 2011 FOCUS Report to reflect the modified capital treatment of the Euro RTMs. The retroactive application of the capital charge to the July 2011 FOCUS Report resulted in a regulatory net capital deficiency of $150.6 million as of July 31, 2011, as compared to the previously reported net capital excess of $104.3 million. As a result, MFGI had to file notices of net capital deficiency with its regulators, the SEC and the CFTC. MF Global also was required to amend its Quarterly Report on Form 10-Q for the quarter ending June 30, 2011. MF Global disclosed the net capital infusion on September 1, 2011 in its Amended Form 10-Q, which stated:

> The Company was recently informed by [FINRA] that its regulated U.S. operating subsidiary, MF Global Inc., is required to modify its capital treatment of certain repurchase transactions to maturity collateralized with European sovereign debt and thus increase its required net capital pursuant to SEC Rule 15c3-1. MF Global Inc. has increased its net capital and currently has net capital sufficient to exceed both the required minimum level and FINRA's early-warning notification level. The Company does not believe that the increase in net capital will have a material adverse impact on its business, liquidity or strategic plans. In addition, the Company expects that its regulatory capital requirements will continue to decrease as the portfolio of these investments matures, which currently has a weighted average maturity of April 2012 and a final maturity of December 2012.

To free up capital at MFGI in response to FINRA's regulatory capital charge, MFGI transferred to FinCo through a reverse RTM ("**RRTM**"), and off of MFGI's books, $4.2 billion of Italian bonds, thereby transferring the risks associated with these positions to FinCo. This allowed MF Global to transfer risk from MFGI, a regulated entity, to FinCo, an unregulated

entity, freeing up regulatory capital at MFGI and lowering the resulting default risk charge required by FINRA.

The Company also took other measures to provide capital relief to MFGI, including selling the London and Asia Pacific affiliate clearing businesses to Bank of New York Mellon Corporation ("**BONY"**) and transferring certain of PSG's positions to a non-regulated entity called MF Global Special Investor LLC.

The increased regulatory demands impacted other aspects of MF Global's business. FINRA limited MFGI's underwriting activities to "Best Efforts" transactions only, instructing MFGI not to conduct any "Firm Commitment" underwritings until the perceived risk of the Euro RTMs was sufficiently reduced. On September 19, 2011, FINRA also placed MFGI on special surveillance and requested that the Company provide it with certain financial information on a weekly basis, due to the "overall risk undertaken by the Company in maintaining the inventory levels" in Euro RTMs. In addition, the Office of the Comptroller of Currency (the "**OCC**") asked MFGI to explain why it had failed to provide the OCC with an Early Warning Notice regarding FINRA's decision to require MFGI to increase its net capital requirements. The New York Fed inquired about FINRA's net capital decision, the Company's net capital calculation for MFGI, and other risks.

4. FSA's Reaction to the Capital Charge

MFG UK's regulator, the FSA, also began raising concerns about MFG UK's exposure to the Euro RTMs. By August 2011, the FSA instructed MFG UK to prepare a contingency plan for liquidity stresses arising from the Euro RTMs. The FSA required detailed information on the positions, stress testing, and liquidity, including the impact of the reduction in value of the

collateral being used for margin calls, group-wide stress scenarios being performed, and any mitigating actions by management. The FSA told MFG UK that it was uncomfortable with MFG UK's liquidity position and with its intraday liquidity position and focused on what would happen if MFGI failed to fund MFG UK to meet an intraday Initial Margin call from LCH.

5. The Press and the Credit Rating Agencies React to FINRA's Capital Charge Decision

An October 17, 2011 article in the Wall Street Journal titled "MF Global Told to Boost Capital" reported these developments with MF Global's regulators. While stating that the Company was "able to quickly remedy the situation, increasing its capital above required levels" and that there was no sign that MF Global had a liquidity problem, the article stirred the credit rating agencies into action and focused the market on the Company's large exposure to Euro RTMs.

H. The Final Week of MF Global's Operations

1. Monday, October 24, 2011

On October 24, 2011, Moody's downgraded Holdings Ltd. to near-junk status, to Baa3 from Baa2, and placed it under review for a further possible downgrade, stating: "MF Global's increased exposure to European sovereign debt in peripheral countries and its need to inject capital into its [B/D] subsidiary to rectify a regulatory capital shortfall highlights the [Company's] increased risk appetite and raises questions about the [Company's] risk governance."

That same day, Steenkamp wrote an email to S&P stating MF Global's "capital and liquidity has never been stronger," and that "MF Global is in its strongest position ever as [a] public entity."

In response to activity by the rating agencies, the Audit and Risk Committee met and agreed that the Holdings Ltd.'s quarterly earnings announcement should be moved up to October 25, 2011, in order to facilitate providing the market with additional information.

At this time, Stockman also listed the Company's net funded exposure to IPSI debt at $7.687 billion and $422 million for Belgium and France. The Company drew $230 million on its unsecured RCF that day.

2. Tuesday, October 25, 2011

At an early morning meeting on October 25, 2011 with Operations Department personnel called by Abelow, he indicated that the Company's management had decided to try to liquidate securities to generate liquidity. Bid lists were sent to JPMorgan Chase ("**JPMC**"), Goldman Sachs, BONY, and others, offering a laundry list of securities that MF Global was looking to sell. Potential buyers responded with prices for those trades, and Operations Department personnel worked to execute the trades as they came in.

On October 25, Holdings Ltd. also announced its results for the second fiscal quarter ended September 30, 2011, posting a $191.6 million GAAP net loss, compared with a loss of $94.3 million for the same period the prior year. The net loss reflected, among other things, a write-off of valuation allowances that had been taken against deferred tax assets, which accounted for $119.4 million of the $191.6 million in GAAP net loss, as well as a decrease in net revenue primarily due to the contraction of proprietary principal activities. That same day, the Company's stock price fell by 48 percent.

During an earnings call on October 25, 2011, Corzine and Steenkamp continued to highlight what they claimed was the Company's strengthened liquidity and capital profile.

Corzine represented that management had “substantially improved our capital and liquidity positions” and “husbanded our capital and strengthened our liquidity.” Steenkamp also stated that “the capital market transactions this quarter improved [the Company’s] capital and liquidity positions,” its “capital structure has never been stronger,” and that management felt “good about [the Company’s] capital structure and liquidity position as well as the strategic direction and progress against the plan.”

Despite these assurances, the public responses to the earnings announcements and downgrades were negative. The FCM’s client with the largest segregated and secured balances announced that it was pulling its money out of the FCM due to the downgrade. MFG UK received a margin call from LCH for 110% margin as a result of the downgrade. Holdings Ltd. also drew down an additional $300 million on its unsecured RCF to ease the Company’s growing liquidity pressures.

The weaknesses in MF Global’s operations systems also were having a manifest impact on its business. Fail reports that indicate whether trades reaching their settlement dates have not yet settled, significantly increased on October 25, but these reports were unreliable. The system fail reports were defective in that: (1) they showed false positives (*i.e.*, they reported trades that had not reached their settlement date); and (2) they did not provide adequate descriptions for the reasons why trades failed. These system deficiencies required Operations Department personnel to engage in a manual process of generating the records necessary to clear and settle transactions, such as by exchanging emails. The manual nature of this process made clearing and settlement more difficult in the final week of the Company’s existence, when literally hundreds of transactions had to be handled through this manual process.

3. Wednesday, October 26, 2011

On October 26, 2011, S&P placed Holdings Ltd. under a CreditWatch with negative implications, taking note of the Company's outsized exposure to European sovereign debt in relation to its capital base:

> We believe that the [C]ompany's future business plans could entail increased risk taking as it transforms itself into a full-service investment bank. For example, the [C]ompany has disclosed its exposure to certain European sovereign debt, which amounts to approximately $6.3 billion and represents 5.2x the [C]ompany's total equity. We consider this exposure to be very high, compared to the [C]ompany's loss absorbing capital base. MF Global entered these short-term repurchase agreements as a means to facilitate client trades. Although trades such as these can diversify the [C]ompany's revenues from its traditional brokerage business, in our view, they also increase the [C]ompany's risk profile.

MFGI's regulators also started engaging personnel to understand what was happening. Corzine participated in two calls with the New York Fed. Laurie Ferber ("**Ferber**"), the Company's General Counsel, received a call from the SEC to arrange a meeting to discuss liquidity and funding issues with both the SEC and CFTC.

In order to meet the need for additional liquidity at the B/D, on October 26, MFGI transferred $615 million from the FCM. Because the Company was unable to monitor segregated funds in real time, members of the Treasury Department were not certain, even after the close of business, whether the $615 million came from customer funds.

This uncertainty is highlighted in emails from Edith O'Brien ("**O'Brien**"), MFGI's Assistant Treasurer, to members of the Operations Department, including Richard Gill, David Lyons, and David Simons, in which she stated: "I NEED TO KNOW HOW MUCH IS BEING RETURN[ED] — FROM WHERE TO WHERE" and "**I NEED TO KNOW NOW — TO PRE-ADVISE FUNDING AND AVOID A SEG ISSUE**." (Emphasis in original.) The

Company's Operations Department personnel, however, failed to return any funds before the end of the day.

Either late Wednesday night (October 26) or early Thursday morning (October 27), O'Brien and Jason Chenoweth, who worked in the Treasury Department, discussed the concern that customer segregated balances may have gone negative during the day. Their lack of comfort was exacerbated by the Company's lack of real-time monitoring of segregated funds. The Securities Investor Protection Act ("**SIPA**") Trustee's investigation revealed that MFGI experienced a customer fund shortfall beginning October 26, 2011, even though MFGI personnel may have believed they were still in regulatory compliance.

The Company continued to experience extreme liquidity stresses during the final week of its existence. LCH issued additional margin calls as a result of the downgrade. At the same time, a substantial volume of securities could no longer be funded through the third-party repo markets and were left "in the box," meaning MF Global had to fund them on its own, which decreased available liquidity. The volume of the securities "in the box" increased from $199 million on October 21 to $606 million on October 26.

By the end of the day (October 26), MF Global had drawn down $223.1 million from its unsecured RCF in order to address growing liquidity stresses.

The Company's efforts to sell its Euro RTM portfolio suffered a setback when Abelow brought a representative of the investment bank Jefferies & Company ("**Jefferies**") to meet with Corzine to discuss selling the portfolio. Corzine refused to meet with the representative because he was in the process of auctioning some commercial paper, and needed to complete the sales

before the close of the London market. Consequently, no sale of the Euro RTMs was discussed with Jefferies at this time.

In light of the week's events, MF Global formally retained Evercore Partners Inc. to assist with efforts to sell all or part of the Company.

4. Thursday, October 27, 2011

On October 27, 2011, Fitch downgraded Holdings Ltd. to BB+ from BBB and placed it on a negative rating watch, observing:

> These increased risk taking activities have resulted in sizeable concentrated positions relative to the [Company's] capital base, leaving MF vulnerable to potential credit deterioration and/or significant margin calls. While Fitch notes that the [Company] has made some progress in rationalizing its capital structure, the [Company's] persistently weak earnings and leverage are no longer consistent with an investment grade financial institution.

Moody's also downgraded Holdings Ltd. by two notches to Ba2 from Baa3, cutting Holdings Ltd.'s credit rating to junk status, explaining:

> [T]he downgrade reflects our view that MF Global's weak core profitability contributed to it taking on substantial risk in the form of its exposure to European sovereign debt in peripheral countries. At the end of the second quarter, MF Global's $6.3 billion sovereign risk exposure represented 5 times the [Company's] tangible common equity.
>
> "The tactical decision to assume this outsized proprietary position, highlights the core profitability challenges faced by MF Global and the scope of the re-engineering challenge facing the [Company's] management," said [a senior Moody's analyst.]
>
> Moody's believes that the risk appetite revealed by this position, in tandem with the significant quarterly loss that MF Global reported, subjects the [Company] to a heightened risk of loss of client and counterparty confidence — and could thus further challenge the [Company's] franchise.

Not surprisingly, the rating downgrades were followed by an increase in margin calls against MFG UK, which were passed on to MFGI, a further exodus of its customers, and increased activity by MFGI's regulators. Corzine participated in numerous calls with the New York Fed and representatives from the SEC and CFTC, who met to discuss the challenges facing the Company, including liquidity measures, funding sources, the Euro RTM portfolio, available collateral, what liquidity stress tests had been performed, changes to margins, and the commodities segregation calculation.

Personnel from JPMC, which cleared much of MF Global's trading, also were present at the Company's offices throughout October 27, reviewing and approving each instruction for settlement of a securities transaction to determine whether to permit it to settle. JPMC put Holdings Ltd. on "debit alert," which mandated that requests to transfer funds would not be executed unless the bank determined that there were "good funds" present in the account adequate to support the requested transfer. JPMC also terminated all of Holdings Ltd.'s uncommitted intraday credit lines.

During the day, Christine Serwinski ("**Serwinski**"), MFGI's North American CFO, learned that the segregation report for Wednesday (October 26) showed a substantial deficit in the "Firm Invested In Excess" balance. These are amounts deposited by the Company in the FCM's customer accounts to help prevent those accounts from becoming under-segregated due to market events. When she received a copy of the internal Daily Segregation Statement ("**Segregation Statement**"),[14] Serwinski emailed O'Brien, asking for an explanation for a large negative Firm Invested in Excess balance and expressed concern about a $200 million inter-

[14] The Segregation Statement was required to demonstrate that assets on deposit in customer segregated accounts were in compliance with CFTC Rule 1.20.

company transfer (described as a "loan") from the FCM that had been made on October 27. O'Brien responded that the transfer was not a loan, saying, "'Lent is a strong word' I would state -- Fail to return intraday funding compounded by Funding B/D Customer Wires." O'Brien explained that the erosion of the Firm Invested in Excess from October 25 to October 26 was due to $80 million in outgoing securities customer wires and $290 million in two inter-company transfers that the Operations Department personnel in New York failed to repay, which decreased the balance by a total of $328 million. O'Brien also informed Serwinski that she estimated the Firm Invested in Excess would be negative $167 million as of close of business on October 27, 2011.

In an attempt to meet increasing liquidity drains, the Company drew down an additional $52.1 million on the unsecured RCF, attempted to liquidate a portion of the hold to maturity ("**HTM**") portfolio (which invested the Company's own money and was funded via the B/D) and sold a large volume of commercial paper to Goldman Sachs. By October 27, the $1.2 billion unsecured RCF was almost fully drawn, with the exception of $27 million that one of the banks refused to fund.

MFGI also tapped its $300 million secured RCF for the first time. However, there were no automatic procedures in place to make sure that the right collateral was placed to cover the amounts sought from the RCF. As a result, the wrong collateral was often pledged and rejected by the syndicate banks, leading to a further slowdown of clearing and settling operations.

By October 27, the Company made a strategic decision to shrink the balance sheet.

5. Friday, October 28, 2011

By October 28, 2011, MF Global was struggling to free up liquidity in order to keep the Company afloat. As a result of debit caps and other hurdles imposed by the clearing banks, the Operation Department was hampered severely in executing trades. In an email, Simons informed Abelow that clearing and settlement activities were moving very slowly with JPMC and BONY.

At the close of business on the previous day (October 27), MFG UK had overdrawn several of its accounts with JPMC by approximately $175 million. MF Global was trying to sell roughly $5 billion in bonds to shrink the Company's balance sheet to generate liquidity, but JPMC informed Corzine that it would not engage in additional transactions until the overdrafts in London were cleared up. In an e-mail, Mahajan explained that JPMC was "HOLDING UP VITAL BUSINESS IN THE US AS A RESULT" of the overdrawn UK account. Corzine contacted MF Global's Chicago office and asked them to resolve the overdrafts.

To cover the overdrafts, O'Brien approved and processed a $200 million wire transfer from one of MFGI's customer segregated accounts to an MFGI account, and then authorized the transfer of $175 million from that account to an MFG UK account at JPMC in London.

The Financial Regulatory Group's preliminary review of the segregated and secured calculations as of the close of business on October 27 uncovered a $300 million deficiency in the Company's segregated accounts. After discussions with Chenoweth, Hughey determined that the deficiency was the result of five transactions totaling $540 million that had been booked incorrectly. Financial Regulatory Group staff members thereafter manually adjusted the Company's segregation statement by $540 million in the absence of back-up for that adjustment

from the Treasury Department, resulting in a $200 million surplus in segregation on the reports filed with the regulators.

6. Saturday, October 29, 2011

By Saturday, October 29, a deficit of almost $1 billion in customer funds was identified during the Financial Regulatory Group's preparation of the FCM's segregation statement. The individuals working on the segregation statement speculated that the manual adjustment of $540 million posted a day earlier, on Friday, October 28, 2011, must have been incorrectly booked backwards (*i.e.*, $540 million had been debited from segregation instead of credited), but they were unable to confirm that the discrepancy was simply a bank reconciliation error. One of those individuals, Hughey, emailed Serwinski stating, "Seg and Secured apparently OK — Treasury assures us we have excess seg. Waiting for Treasury to provide support and backup for adjustments."

The Treasury Department also assured Serwinski that the segregation and Daily Secured Statement (the "**Secured Statement**")[15] for October 28 showed MF Global to be under-segregated as a result of a reconciliation error.

In an effort to confirm that the overdraft transfer did not involve customer funds, JPMC requested that MF Global sign an assurance letter. After O'Brien was reluctant to sign the letter, its scope was narrowed to the two transactions at issue, which Ferber reviewed and deemed satisfactory. Although O'Brien indicated she was comfortable signing the narrower version of the letter, she ultimately did not sign it.

[15] The Secured Statement is the daily statement demonstrating that assets on deposit in foreign secured accounts were in compliance with CFTC Rule 30.7.

Later in the day on October 29, Mahajan, O'Brien, Dennis Klejna ("**Klejna**"), MFGI's Assistant General Counsel, and Michael Bolan ("**Bolan**"), MFGI's Global Product Controller, participated in a conference call to discuss signing the letter. O'Brien indicated that when she made the $175 million transfer, there were sufficient funds to cover the transfer. Mahajan expressed his willingness to sign the assurance letter if O'Brien provided him with some additional information confirming this fact. However, at that time, the final customer segregation computations were not available.

At a special meeting of the Board held that evening, Abelow reported that the Company experienced significant difficulty on Thursday (October 27) and Friday (October 28) maintaining the liquidity necessary to conduct trading activities in the ordinary course because some of its clearing banks were not releasing excess margin and other cash owed to the Company without significant delay or in some cases at all. Because JPMC and other banks had shown an interest in acquiring the Company's Euro RTM portfolio, the Board encouraged management to request bids for this portfolio as well as other trading portfolios (including government agency positions and corporate positions) for settlement by Monday (October 31) and to make recommendations to the Board by Sunday (October 30) as to which transactions to pursue. The Board also heard a presentation on bankruptcy issues.

7. Sunday, October 30, 2011

By Sunday, October 30, 2011, word had spread throughout the Company that MF Global's customer accounts were short by almost $1 billion. Serwinski believed this deficit was the result of an accounting error. She and others working under her supervision continued to try to verify the segregation numbers in order to identify the perceived accounting error.

Regulators also continued to pressure MF Global for information regarding the segregated and secured numbers, which MF Global could not provide. MF Global employees worked throughout the day to confirm the numbers, missing deadlines set by the CFTC and the CME. Late in the evening, the Board was informed that MF Global employees had not been able to resolve the deficit in the customer segregated accounts.

8. Monday, October 31, 2011

Early on October 31, 2011, MF Global reported to its regulators a $952 million deficit in segregated funds as of the close of business on October 28. As a result of the deficiency, a potential sale of the Company collapsed and Holdings Ltd. and FinCo filed for bankruptcy.

I. Debtors' Funds at the Commencement of the Bankruptcy Cases

As of October 31, 2011, approximately $26 million remained in a JMPC bank account, number XXXXX3683 (the "**JPM Account**"), maintained by FinCo. During the December 9, 2011 omnibus hearing, the Court expressed concerns regarding whether the JPM Account contained any funds of MFGI's customers. On December 14, 2011, the Court directed the Trustee and his advisors to complete a forensic analysis of these funds and to provide the Court with a report regarding the Trustee's findings. The Trustee filed this report on February 16, 2012 [Docket No. 451] (the "**60-Day Report**").[16]

Led by FTI, the Trustee's advisors reviewed bank and transaction records pertaining to cash inflows into the JPM Account in preparation of the 60-Day Report. The purpose of the

[16] On December 14, 2011, the Court issued the Memorandum Opinion Approving use of Cash Collateral on a Final Basis, and the Final Order Under 11 U.S.C. §§ 105, 361, 362, 363(c), 363(e) and 364 and Bankruptcy Rules 2002, 4001, 6003, 6004 and 9014 (I) Authorizing the Debtors to Use Cash Collateral, and (II) Granting Adequate Protection, which contained the official mandate that the Trustee complete the forensic analysis and provide the Court with findings in the 60-Day Report.

analysis was to determine whether these cash inflows represented any of the "missing" cash of MFGI's customers. The investigation focused on transactions in and out of the JPM Account during October 2011, because the Trustee believed that the irregularities with respect to customer property did not occur prior to October, as indicated in the SIPA Trustee's February 6, 2012 report.

On October 1, 2011, the JPM Account had a balance of approximately $32 million and on October 28, 2011 the JPM Account had approximately $26 million. During that time, nearly $1.762 billion flowed into the JPM Account and $1.769 billion flowed out.[17] Cash flowed into the JPM Account from limited sources.[18] Although in excess of $1.76 billion flowed into the JPM Account from various sources during October 2011, only $33.5 million originated from an MFGI bank account that contained customer funds (the "**Customer Funding Account**"). An additional $950 million flowed into the JPM Account from borrowings made under the unsecured RCF during October 2011. These inflows were carefully reviewed by FTI.

All transactions between the Customer Funding Account and the JPM Account were the result of loans made by FinCo to customers to cover margin calls. Those loans were made from the JPM Account into the Customer Funding Account for the customers' benefit. Margin loan repayments were made from the same Customer Funding Account by MFGI on behalf of specific customers, thereby reducing the customers' respective outstanding obligation to FinCo.

[17] On October 13, 2011, the balance in the JPM Account fell to $148,424 as of the close of business. This low balance provides further proof that the investigation of whether or not the "missing" customer funds were being held by the Debtors after the commencement of Holdings Ltd.'s and FinCo's bankruptcy cases need not extend before October 1, 2011. In doing the tracing analysis as to the "missing" funds after bankruptcy, this low balance in an account that processed transfers of hundreds of millions of dollars at a time is the equivalent of starting with a balance of $0.

[18] For a more detailed accounting of all of the inflows and outflows in the JPM Account, see the 60-Day Report attached as Appendix D.

During this same period, FinCo made customer loans into the Customer Funding Account of more than $44 million. In other words, the Customer Funding Account received from the JPM Account more than $10 million on a net basis during the month of October 2011. Other than payments from the Customer Funding Account as described above, there were no other instances of any payment from an MFGI customer segregated account into the JPM Account.

Of the more than $1.76 billion in inflows into the JPM Account during October 2011, more than $950 million is attributable to receipts from Holdings Ltd. This sum represents borrowings made under the unsecured RCF during the month of October 2011. These inflows cannot be tied to customer cash. In addition, a review of the cash inflows from other sources (mostly, unregulated FinCo affiliates) does not reveal any segregated MFGI customer funds coming into the JPM Account.

Therefore, based upon: (a) a careful analysis of JPM Account activity during the month of October 2011, (b) the review of numerous documents from the Debtors and affiliates' files, (c) the analysis of bank statements and other records provided by the SIPA Trustee's representatives, and (d) interviews conducted by FTI of MFGI employees, the Trustee determined that the JPM Account did not contain any cash that should have been held in customer segregated accounts. The SIPA Trustee advised the Trustee that he agreed with the conclusion reached in the 60-Day Report that the cash in the JPM Account, as of October 31, 2011, did not appear to include misappropriated MFGI customer funds. Further, neither the Trustee nor the SIPA Trustee are aware of any evidence indicating that the JPM Account contained misdirected or misappropriated MFGI customer funds.

III. MANAGEMENT'S ROLE IN THE COMPANY'S COLLAPSE

Corzine's vision for MF Global, to transform the Company from a traditional FCM to a sophisticated B/D and full service investment bank, did not take into account MF Global's deficiencies. MF Global's problems stemmed in part from the Company's disorganized global structure, which one former executive described as loosely cobbled together from a matrix or overlay of regional and product groups. Before Holdings Ltd. went public, it acquired several disparate companies that it never properly integrated. As one subordinate wrote to Corzine in April 2010, "[t]here is little business or dispositional integration between the many offices and branches. There is, in short, no house culture."

The unwieldy corporate structure lacked cohesion both in its culture and in its operating structure. Even after the changes made to its risk and control systems after the Dooley incident, MF Global's systems had serious deficiencies that posed problems for the Company even as a traditional FCM. When Corzine's vision was implemented, the Company's deficiencies were exposed in a number of ways:

(1) there was no efficient, concise way for anyone at the Company to have an accurate and complete real-time snapshot of the Company's most basic financial information, including liquidity;

(2) inefficient and outdated control systems were inundated as trading increased, crippling the settlement and clearing of trades, which became a decisive threat to MFGI's ability to function during the last week of October 2011; and

(3) the inability to forecast and track financial information accurately on a real-time basis resulted in executive management reacting too late and too slowly to the growing liquidity pressures placed on the Company by the Euro RTMs and Corzine's new trading desks.

As early as May 2010, Corzine and Steenkamp knew that MF Global's control architecture was flawed. Gaps between approved risk and control policies and current practices were documented, distributed to management, and presented to the Board. Repeated warnings about the Company's control systems put management on notice that the Company did not have the appropriate systems in place to support the expanded trading Corzine envisioned when he joined the Company.

Instead of heeding the warnings, management began to execute Corzine's vision, hiring traders without giving thoughtful consideration or analysis as to whether the control and back-end systems could support those new products and trading desks.

At the same time that the Company faced increasing margin demands to support the Euro RTMs, it had to expend considerable resources to support the addition of new trading desks that dealt in securities that the Company could not finance. The Company had to find ways for MFGI to operate with the substantial regulatory capital charges imposed by U.S. regulators, including increasingly relying on the FCM for daily cash infusions to the B/D. Throughout this time, management harbored a mistaken belief that the two RCFs were a sufficient and appropriate backstop to cover the Company's liquidity needs.

Meanwhile, as an FCM, MFGI was required by law to hold significant amounts of capital compared to MF Global's equity. As time passed and the Company's proprietary trading grew more complex and involved more illiquid securities and instruments, capital became increasingly trapped. As a result, MF Global was capital rich but liquidity poor.

In short, MF Global was on shaky ground long before the events of October 2011. Corzine and management knew, or should have known, that these factors were contributing to a precarious liquidity position that ultimately spelled disaster for MF Global.

A. MF Global's Control Failures

Corzine and the heads of the Finance, Risk, Operations, and Treasury Departments understood the importance of having functioning risk and control systems, and that those systems must be commensurate with the Company's risk appetite. Management knew that the Company required an enhanced control and risk management architecture to expand trading activities and transform MFGI's FCM model to a B/D and later to an investment bank. Corzine expressed this practical reality to the public:

> We intend to control and manage risk. . . . Our strategic review is not just about our retail business, not just about how we organize our institutional sales or our trading activities, but it's also about how we maintain proper control and compliance as we go forward.

1. Management Learned About Significant Gaps Between Risk Policies and Actual Practices Before Expanding MF Global's Proprietary Trading Activities

MF Global's officers were placed on notice about the defects in the Company's controls before the first Euro RTMs were entered. In March 2010, the same month that Corzine joined MF Global, the Board asked management to prepare an analysis of gaps between the documented and approved Risk Policy and current practice. At the May 27, 2010 meeting of the Audit and Risk Committee of the Board, management gave a presentation dated April 2010 (the "**April 2010 Gap Analysis**"), which showed dozens of gaps between the Company's written risk control policies as described in the Risk Policy and the Company's actual risk control practices.

The April 2010 Gap Analysis identified the following weaknesses, among others, as "high" priority risks:

(1) liquidity risk scenario analyses and stress tests were not yet developed; and

(2) the Treasurer lacked the appropriate systems and technology to conduct independent liquidity monitoring and forecasting.

The April 2010 Gap Analysis also identified the following weaknesses, among others, as "moderate" priority risks:

(1) no return on risk-adjusted capital was being generated due to the lack of global economic internal capital-based performance measures;

(2) the Company failed to hire someone to fill the important role of Global Head of Capital & Liquidity Risk; and

(3) the Company failed to develop the LRMD, which was supposed to document the Company's contingency funding plan.

In October 2010, Roseman gave the Audit and Risk Committee a status update on the numerous gaps between the Company's policies and practices identified almost half a year earlier ("**October 2010 Gap Analysis**"). Out of thirty-two gaps previously identified, only two had been resolved, and all of the high priority gaps persisted. Some high risk areas, such as the need for liquidity risk scenario analyses and stress tests and return on risk-adjusted capital remained "under development." Gaps in economic capital risk measurement, liquidity risk scenarios and operational risk profile were raised to "critical" priority status. The October 2010 Gap Analysis faulted "reduced staffing and budget" as "key challenges to policy-gap remediation progress." Additional challenges noted by the October 2010 Gap Analysis included "[l]ow

staffing levels in the Risk department" and "[d]iminished information technology project budget and resources."

Also in October 2010, a report prepared by Internal Audit on "Market and Credit Risk Management" identified "High Risk" areas arising from the lack of controls over risk reporting. The report emphasized that market risk policies had not been updated to reflect MF Global's then-current operating environment.

In June 2011, more than a year after being alerted to these control deficiencies in the April 2010 Gap Analysis, Internal Audit again alerted management to limitations in the Company's ability to track liquidity. According to the June 2011 Global Liquidity and Capital Management Internal Audit Report (the **"June 2011 Internal Audit Report"**), "[e]xisting liquidity monitoring and forecasting is manual and limited. Reporting capabilities to evaluate liquidity needs for transactions that are booked but not yet settled have not been fully developed." The report further found that "[e]xisting performance of formal stress testing and scenario analysis is not adequate to fully assess liquidity and capital needs."

The June 2011 Internal Audit Report also identified a "key man" risk in connection with liquidity reporting, monitoring and forecasting tools, specifically noting that "[t]he lack of formal reporting, monitoring and forecasting creates an unnecessarily high reliance on key employees and increases the risk exposure should these staff members leave the Company." The Internal Audit work papers underlying the June 2011 Internal Audit Report specifically discussed the fact that the forecasting was not documented and was based mainly on the expertise and experience of a single employee in the Treasury Department, MFGI's Assistant Treasurer, O'Brien, presenting this "key man" risk.

The June 2011 Internal Audit Report assigned responsibility to Steenkamp and Abelow, and other officers who reported to them, for resolving these issues, many of which were never resolved before the Company collapsed. The June 2011 Internal Audit Report warned that:

> The complexity of capital and liquidity demands have increased with the addition of principal trading across the [Company's] customer facing desks, the principal strategies group, and other previously approved new businesses. These additional stresses further emphasize the need for a more formal and consistent approach to liquidity and capital management.

Despite having specific knowledge about these risks, management appears to have done very little to address them. For example, the June 2011 Internal Audit Report stated that management accepted the "key man" risk: "[t]he business accepts this risk and a formal action plan will not be tracked. The implementation of the other planned solutions in this report will serve to mitigate much of the existing key man risk." The "other planned solutions" referenced included fixing some of the other major gaps identified in May 2011, such as automating liquidity reporting, documenting the Company's global contingency funding plan, and creating stress testing to evaluate the impact of specific scenarios on the Company's liquidity and capital.

Nevertheless, these projects remained incomplete at the time of the Company's collapse. In addition, by the time MF Global collapsed, no formalized process for approving new business initiatives, including funding such initiatives, and no method of managing and responding to capital requests from the individual trading desks had been established.

Despite the warnings, MF Global did not adequately bolster the control environment, even as Corzine's ambitious strategy was put into high gear. Risk Department officials made some efforts to develop the liquidity risk scenarios (described in the Risk Policy), but those scenarios were still "in progress" as late as October 2010. By December 2010, development of

those scenarios had stalled, largely due to what one former Risk Department executive called the lack of "buy-in" by officials in the Treasury and Finance Departments. Even though the process of developing these scenarios continued again during the summer of 2011, development of one of the scenarios was not complete until the "Break the Glass" analysis was presented to the Board in October 2011.

As the business transformed in 2011 to fit Corzine's long-term vision, management did seek changes to its risk policy documents to reflect changes in the nature of the Company's business. An August 11, 2011 presentation to the Board noted that management anticipated raising the Company's risk appetite and Delegations to reflect the Company's "current strategy and risk profile." In acknowledgement of the repeated breaches of internal capital limits (discussed below), these changes included a proposal to lower the internal capital threshold. The changes were intended to increase the Company's risk appetite "from [the] conservative profile of an FCM to the profile of a broker-dealer" and were "[e]xpected to reduce [the] number of limit breaches raised to [the] Board that do not reflect true risk management concerns."

2. Specific Control Failures

MF Global's collapse was abetted by, among other things, management's failure to integrate or upgrade its various technology systems and platforms for monitoring Treasury Department operations, liquidity risk, and financial regulatory functions. These systems were left without proper controls even as the Company substantially expanded its proprietary trading under Corzine.

a. Lack of Liquidity Monitoring and Forecasting – Liquidity Dashboards

The Treasury Department lacked the appropriate systems and technology to conduct accurate liquidity monitoring and forecasting across the global operation. MF Global's continuing problems monitoring, gathering, and reporting accurate financial data limited the Company's ability to manage the increased liquidity pressures.

The problems were apparent on August 21, 2011, when Mahajan sought a basic report of monthly cash flows. Mahajan first turned to Steenkamp, to ask for a cash flow projection report. Steenkamp replied that although this was something the Company had always wanted, the Treasury Department did not have the ability to monitor cash flows and create such a report. He suggested that a Finance department employee, Aviva Nussbaum ("**Nussbaum**"), might be able to get Mahajan the information he sought. Mahajan emailed Nussbaum the next day, again seeking a basic report of monthly cash flows. The Finance Department could not produce even a high level overview of cash flows for a period of a month or two. Nussbaum responded that the complexity of the business did not allow the Finance Department to create such a report and that the Finance Department did not have the systems to generate it. Mahajan continued to push for the information, but ultimately never received it before Holdings Ltd. and FinCo filed for bankruptcy.

Even though this risk was identified as early as March 2010, MF Global's management did not begin to discuss hiring a vendor to develop an integrated global treasury system until July

2011. The vendor selection and implementation phase was scheduled to take place in February 2012, which turned out to be four months after the Company's collapse.[19]

A Finance Department executive described the Treasury Department's systems as a "hodgepodge of systems and processes without a design." Lacking a robust cash management or liquidity forecasting system, the Treasury Department often lacked insight into what was needed and when it was needed. Additionally, the Company lacked a tool to monitor leverage before the end of the quarter, despite the fact that leverage was one of the areas of focus for the credit rating agencies and analysts reviewing the Company's performance.

The lack of coordination between the Finance and Treasury Departments also prevented the Company from properly tracking its cash. In one instance, the Treasury Department transferred $25 million to finance an Asian currency trade without providing any advance notice to the Finance Department. The Finance Department later decided to take a 100% capital charge on the trade when it did not get an adequate explanation about the transfer from the Treasury Department.

Because the Treasury Department lacked appropriate systems for managing cash movements, the Finance Department often needed to correct the Company's accounting books and records manually to make sure they were accurate. Finance Department employees reported these concerns about the Treasury Department's systems in a March 2011 controls report made to Steenkamp pursuant to the Sarbanes Oxley Act of 2002.

[19] A planned overhaul of the treasury systems used by MFG UK was discussed and eventually implemented in 2010. MFG UK spent millions of dollars on the "S&P Lombard" system, which helped the UK affiliate better track its liquidity on a daily basis, but the Company never overhauled its global treasury systems.

The failure to integrate personnel and operations adequately exacerbated the problems created by the Company's deficient systems and technology. When Mahajan joined the Company as Global Treasurer in August 2011, he was based in New York, even though most Treasury Department employees were located in Chicago.[20] O'Brien, as Assistant Treasurer under Mahajan, was located in Chicago and was responsible for approving transfers from the FCM and monitoring the effect of those transfers on MFGI's regulated accounts. Responsibility for the processing of these transfers, performing bank reconciliations and executing wire transfers and other money movement fell under a group separate from the Treasury Department called Treasury Operations. Treasury Operations, including a team of ten individuals based in Chicago, reported to MFGI's North American COO, Robert Lyons, who was based in New York.

Employees in New York and Chicago failed to communicate adequately about intraday funding requests or use of transferred funds. Treasury Department and Treasury Operations personnel were frustrated by the lack of communication, the increasing reliance on the FCM to fund other parts of the business and the lack of transparency once transfers were made out of the FCM. Treasury Operations personnel located in New York, for their part, needed funding to maintain operations, but were not aware of the source of the funds other than that the funds originated with transfers from the Treasury Department in Chicago.

In the absence of an automated global treasury system, the Company relied on the work of key Treasury officials, led by O'Brien, to (1) manually track the movement of money between the Company's legal entities and (2) provide a daily snapshot of the Company's global liquidity

[20] Mahajan had significantly more experience managing treasury functions in a global banking operation than did his predecessor, David Dunne ("**Dunne**").

position and the sources and uses of liquidity for the B/D. The reports that the Treasury Department prepared, eventually referred to as the "**Liquidity Dashboard**," were usually compiled by Matthew Besgen ("**Besgen**"), a Treasury Department employee based in New York, using data received from various business desks across the Company. At Corzine's request, Besgen began to prepare a daily Liquidity Dashboard in the latter half of 2010. Besgen collated the information from various emails and communications he received from the business desks, the Treasury Department, and the Operations Department. The Liquidity Dashboard was distributed to management, including Corzine, Abelow, and Steenkamp.

The Liquidity Dashboard was the only daily forecasting tool in use to monitor and forecast liquidity needs across the Company. As a threshold problem, the information Besgen used to compile the Liquidity Dashboard was already outdated by the time the report was delivered to management. The Liquidity Dashboard was at best a rough tool. It did not identify the precise sources of the information it contained, and it posed challenges when used to track cash information.

Furthermore, the Liquidity Dashboard provided an overly simplistic and sometimes inaccurate view of the cash available to the B/D. For example, the Liquidity Dashboard treated different types of capital similarly, without explaining that certain types of capital (*i.e.*, working capital as opposed to regulatory capital) are less available for certain business uses than other types, potentially resulting in a misleading report. In addition, the Liquidity Dashboard considered certain funds held by the FCM to be an available source of liquidity, even though, as described below, there are strict rules about what the FCM could do with these funds and it would be improper to construe such funds as available to the B/D.

Although Corzine and others who received the Liquidity Dashboard understood that the figures it contained were estimates and that there were limitations on the information available to prepare the document, as demands on the Company's liquidity increased, they began to use it as the Company's primary liquidity monitoring tool. They did this despite having been warned that the Liquidity Dashboard may not contain timely and accurate information. Besgen also told Corzine during meetings discussing the Liquidity Dashboard that he felt uncomfortable putting the report together because he did not have as much or as accurate information as did others, including the PSG traders (who handled the "front office" functions) and personnel in the Operations Department (who handled the "back office" functions).[21] Besgen felt that this kind of reporting should be the responsibility of the "back office" employees because they dealt with cash issues.

Corzine received the Liquidity Dashboard and discussed it in meetings with Besgen and others (including, on occasion, Steenkamp and Stockman) every weekday. The meetings were focused on the uses and sources of cash. Corzine wanted to know everything that was driving the use of cash and focused on issues such as how the Company could reduce its margin requirements. A topic discussed at these meetings was how and whether MFGI should unwind, or exit, the Euro RTMs.

By the summer of 2011, as the Company's liquidity needs became ever more pressing, the inadequacy of its liquidity monitoring became increasingly problematic. During this period,

[21] The "front office" typically means sales, trading, corporate finance and other public interfacing components of a firm's business. The "middle office" usually refers to risk management, treasury management, internal controls, and corporate strategy components for managing a company's business. The "back office" generally means operations and technology units that ensure smooth settlement of transactions and maintenance of a company's technology systems.

the B/D in New York began to rely on funding from the FCM in Chicago to finance its business. These intraday transfers were recorded through email communications and journal entries, but not in any automated or regular processing system.

b. MF Global Lacked Sufficient Controls Over Regulatory Reporting

The Finance Department was responsible for ensuring that MFGI complied with all of the regulatory requirements associated with its operation of both a B/D and an FCM. Within the Finance Department, the Financial Regulatory Group, which was supervised by Serwinski, was tasked with this responsibility. After May 2011, the Financial Regulatory Group was led by Hughey (under Serwinski). Before Hughey, the job was performed by Jim Marino, who departed the Company in March 2011, leaving the position vacant for almost two months. In preparing the required regulatory reports for the Company,[22] the Financial Regulatory Group relied primarily on spreadsheets and manual calculations.

After Corzine's arrival, the Company invested in upgrading the accounting general ledger system used by the Finance Department. As of January 2011, MF Global spent $12.5 million on replacing the Sun Systems accounting system with the Oracle general ledger system, and budgeted at least $38.1 million for the Oracle system's implementation through the end of fiscal year 2012. This amount represented almost a quarter of the Company's total budget for all systems re-engineering projects in 2011, dwarfing the amounts devoted to the Treasury, Risk, and Operations Departments, as well as other business areas.

[22] These reports included: (1) the Segregation Statement and Secured Statement, (ii) The Net Capital Report, a computation of daily compliance with net capital requirements pursuant to CFTC Rule 1.17, (iii) the 15c3-3 Report, weekly and end-of-month reports regarding compliance with SEC segregation requirements pursuant to SEC Rule 15c3-3; and (iv) the monthly FOCUS report required by SEC Rule 17a-5.

The amounts spent on Oracle were not sufficient to remedy the persistent manual accounting issues. The Finance Department and its employees continued to be frustrated by the lack of a robust general ledger system.

Even though a project implementation team was working to collect suggestions on ways of fixing the system, these technology issues persisted through the time of the Company's collapse. The Financial Regulatory Group continued to experience significant delays in generating the information required of it. The problems with Oracle were pervasive enough that Serwinski and the Financial Regulatory Group reverted to using the Sun Systems accounting system due to data aggregation limitations in Oracle. Management, including Corzine, Steenkamp, and Abelow, were put on notice of serious control deficiencies in the process of gathering information to prepare regulatory reports by a March 2011 Internal Audit Report. The report stated that in reporting proprietary trading information:

> The Regulatory Reporting group handles numerous daily, weekly and monthly reporting responsibilities. The vast majority of the calculations underlying these reports are done via spreadsheet. The group performs various checks and balances to ensure the information utilized is complete and accurate; however, in a variety of instances, the controls are not in place or not all aspects of these controls are documented as evidence that they have been performed. Additionally, these spreadsheets are typically not secure and are susceptible to human error, although at 9/30/10 no material errors were noted.
>
> Further, controls need improvement to help ensure that all accounts with proprietary positions (including error accounts) are identified. Although at 9/30/10, the group appeared to materially capture all proprietary balances in the applicable calculations, better controls for ensuring all proprietary and [Company] owned accounts are captured by Regulatory Reporting need to be implemented, especially as proprietary trading expands within [the Company].

As the B/D's trades became more complex, problems with these manual reporting systems became more pervasive and time-consuming for the Financial Regulatory Group staff, causing delays in reporting. Although notified of these systemic deficiencies as early as May 2011, management had not fixed them by the time of the Company's collapse in October 2011, compounding a shortfall in FCM customer funds that could not be identified soon enough to save the Company.

c. Gaps in Risk System Controls

As discussed in Section II above, the Risk Department implemented a number of improvements after the Dooley incident. Nevertheless, many systemic control deficiencies persisted.

Under Roseman, the Risk Department added to its monitoring and analytic capabilities for assessing the market risks of trading securities and other financial assets with the implementation of Murex, a global market risk system. The Company budgeted almost $4 million for the Murex implementation in 2011. The Company also implemented additional risk management software, RiskMetrics and Risk Informer, which provided automated systems for quantifying stress scenarios under changing market conditions.

However, gaps remained in the Risk Department's monitoring systems even after these upgrades. The Company planned to implement a Global Value at Risk (VaR) system, a necessary measure to enhance the Company's ability to measure the potential economic losses across all portfolios in the event of a stress scenario. This implementation was stalled at the direction of Corzine, who believed that it was unduly expensive.

Even with the limited technology upgrades, the Risk Department faced critical personnel shortages. The position of Global Head of Liquidity & Capital Risk, created in the wake of the Dooley incident, remained vacant, despite Roseman's efforts to fill it. Without a Global Head of Liquidity & Capital Risk, the Risk Department relied on Chaudhry, Global Head of Market Risk, to perform liquidity risk monitoring functions in tandem with the Treasury and Finance Departments. Chaudhry, already occupied with his position, could not fill the critical role of Global Head of Liquidity and Capital Risk.

With key positions vacant and vital roles suffering from a lack of staffing, the June 2011 Internal Audit Report alerted management that "[e]xisting performance of formal stress testing and scenario analysis is not adequate to fully assess liquidity and capital needs." The failure to adequately staff key positions in the Risk Department, not surprisingly, led to a weakness in the performance of formal stress testing and the ability to perform scenario analysis. An October 2010 Internal Audit Progress Report circulated to the Board at its October 27, 2010 meeting more generally noted that staff reductions in the United States had adversely impacted the Risk Department, where key staff had been retained but senior analysts were "covering daily monitoring tasks which [r]educed [the] Risk[] [Department's] responsiveness to business requests and progression of Risk [Department] projects." Simply stated, in addition to relying on inadequate systems, the Risk Department did not have adequate human resources to fulfill its function.

The Risk Department had additional weaknesses with respect to its ability to monitor risk exposures, such as credit and market risk. The October 2010 Internal Audit Report on Market and Credit Risk Management in North America and Europe indicated that "[i]nadequate controls

[were] in place to ensure completeness and accuracy of risk exposure calculation and reporting." The Report assigned a high risk rating to the deficiency and described additional problems with credit and market risk monitoring. Manual processes for monitoring credit and market risk were in need of improvement, and the Risk Department needed to "create workarounds for monitoring risk of client and house positions." End-user computing tools ("**EUCs**"), such as Excel spreadsheets and Access databases, were "necessary to enhance client risk identification and analysis and management reporting of breaches" as "existing Risk systems are not designed for risk exposure calculations and have limited functionality in this respect." Without adequate controls, the EUCs threatened the integrity of the data and created the risk that serious decisions governing the Company's business may be made on inaccurate or incomplete information. The report also assigned unsatisfactory risk ratings to four separate areas related to market and credit risk exposure measurement, monitoring and reporting.

The Risk Department suffered from a number of additional control deficiencies relating to liquidity and capital management. Although these deficiencies were raised as early as May 2010, a June 2011 Internal Audit Report found that management still had failed to correct them:

> (1) the LRMD still was not drafted to provide a formal liquidity management framework and a contingency funding plan;
>
> (2) the Company's adherence to capital utilization limits and communication of corresponding breaches remained inconsistent and not formally managed;
>
> (3) a defined process still was not in place to escalate risk limit breaches that may impact the Company's liquidity and capital needs to management outside of the Risk Department;
>
> (4) management did not have a process in place to shift trading limits to allow principal traders to take advantage of market

opportunities while ensuring the Company stayed within its capital availability; and

(5) capital charges assigned to businesses still did not take into consideration capital utilization limit breaches or the riskiness of their underlying assets, and the charges were not included in the desk level P&L calculations.

d. Operations Department Control Failures

In addition to the control weaknesses identified above, MF Global also failed to put in place a number of controls for managing the expanding portfolio of its B/D.

(i) Use of Two Clearing Institutions

MF Global's B/D operated differently from its competitors, using two clearing banks, JPMC and BONY, instead of just one. Before 2010, MFGI had an exclusive clearing relationship with JPMC. In 2010, MFGI began discussed and nearly finalized a deal to transfer its clearing relationship from JPMC to BONY but ultimately kept the dual arrangement, pursuant to which: (1) BONY would clear U.S. Treasuries trades; and (2) JPMC would clear mortgage-backed securities and agency securities.

It is not clear why MFGI maintained this arrangement or how it benefitted MFGI. Having two clearing institutions was an operational risk, particularly for a company that already was using outdated "back office" systems. This dual arrangement compounded the clearing and settlement complications that materialized in the final week of October 2011, as both JPMC and BONY placed "speed bumps" on trades during the final week, hampering MFGI from accomplishing an efficient and effective liquidation of the Company's securities portfolios that might have allowed the Company to stay solvent.

(ii) Trade Settlement Systems

The problems with MF Global's "back office" systems were exposed in the final week of the October 2011 when the Company struggled to meet its obligations in the wake of the downgrade. In simplistic terms, the Company used various forms of semi-automated journal entry systems to book, clear, and settle trades. Trades were first booked by front-end traders using various trading platforms, including programs called Studio and Phoenix Client. The trading platforms were set up to feed data directly into the "back office" systems for settlement and clearing of fixed income, equities, and other trades. MF Global used a variety of "back office" systems, rather than one global system, for clearing and settlement of trades, including programs such as SunGuard Phase 3, Rolfe & Nolan, and GRIPS.

The "back office" operations systems were antiquated and showed only limited position and account information. For instance, the limitations of Phase 3 were described in a July 2011 Internal Audit report as: "[l]ack of appropriate controls relating to the highly manual processes associated with MBS/TBA trade matching, allocations and settlement of open TBAs."

One of the more problematic aspects of the "back office" systems was that fail reports generated by the systems were defective. As detailed above, the fail reports did not provide the Operations Department with information sufficient to determine why trades that had reached the settlement date failed to settle. These defects and the manual nature of the resulting clearing and settlement processes directly affected the Company's ability to process trades efficiently in the final week of its existence.

In the summer of 2011, the Company's executives investigated potential technology upgrades for its antiquated "back office" systems. One option considered was replacing the

systems with a single state-of-the art platform offered by Broadridge Financial Solutions, Inc. ("**Broadridge**"). However, the Broadridge upgrade was not accomplished before the Company collapsed.

Management also did not take advantage of the option of unifying the various systems within a single platform using the GRIPS system. This solution was available before the Company began its expansive Euro RTM trading strategy, but was not raised until after the size of the Euro RTM positions already had ballooned. In July 2011, Simons asked Verrona Browne, MFG UK's Head of Operations, to finesse the systems used by MFG UK so they could become compatible with the systems used in other foreign affiliates of the Company. This plan remained in the project stage and was not implemented before Holdings Ltd. and FinCo entered insolvency proceedings.

e. Collateral Management Control Failures

The Company's failure to maintain an automated collateral management system also materialized as a significant liability before MF Global collapsed. As the Company began building its principal securities portfolio in 2010 and, in particular, its corporate bond business, it failed to develop an automated collateral management process for tracking securities. The lack of this system ultimately prevented MFGI from being able to clear and settle trades quickly to free up liquidity in the final week of October 2011.

Unlike other financial institutions, the Company did not have a collateral management database to guide Treasury and Operations Department staff on which securities could be pledged to satisfy the conditions of the repo financing agreements. It also did not have a system that automatically identified which customer securities could be pledged.

Instead, the Company would select collateral manually, enter the CUSIP numbers for the securities directly into the clearing bank's technology platform, and then learn post-allocation whether the collateral selected was acceptable under the terms of the relevant agreements.

As a result, instead of being able to rely on an automated system, Operations Department staff spent an inordinate amount of time reviewing repo financing agreements, researching positions, and selecting the appropriate collateral to finance the Company's securities portfolio at a time when the Operations Department already was shorthanded and struggling to fulfill its many other responsibilities.

In addition, the lack of a collateral management database prevented Operations Department personnel from timely drawing upon MFGI's secured RCF, which also required the Company to pledge collateral that satisfied certain contractual conditions.

B. Management Was on Notice that the Company Could Not Adequately Meet its Liquidity Needs

By the summer and fall of 2011, the Company's liquidity problem was one that management could not ignore. The fact that liquidity was disappearing quickly was raised again and again in communications with regulators and internally.

On August 18, 2011, in response to requests from the FSA, Abelow provided liquidity figures showing that the Company had available cash of $410 million, and that MFGI had available cash of $165 million. In mid-September 2011, the FSA requested updated liquidity numbers, and Treasury Department employees discovered that, in less than a month, the Company's available cash had dropped from $410 million to $238 million, and MFGI's available cash had dropped from $165 million to $25 million.

In response to this large drop in liquidity, Treasury and Finance officials directed the Treasury Department to locate additional potential sources of liquidity that could be added to the updated figures being prepared for the FSA in order to make the Company's available cash appear closer to the amounts provided in August. O'Brien identified to Steenkamp a total of $325 million from the FCM and informed Steenkamp that of that amount, $300 million was from segregated funds. When the Company provided the updated liquidity figures to the FSA, it represented that they were "in the same format" as the numbers previously provided, despite the fact that the initial August 18, 2011 submission to the FSA did not include segregated funds in the calculation of total liquidity. Steenkamp approved the use of the updated figures and was aware of the source of the figures provided by the Treasury Department.

Steenkamp outlined the Company's liquidity problems in an October 6, 2011 email to Corzine, Abelow and others.[23] Steenkamp wrote:

> There remains a significant stress on liquidity . . . . Of most concern, is the sustained levels of stress and the lack of signs this will reduce soon. It makes drawdowns of the [RCF] more challenging, as we cannot guarantee certainty of immediate repayment. The [RCF] is not meant as a source of permanent liquidity.
>
> Haircuts and box positions today have continued to increase and were fortunately offset by FCM increases (that is not controllable). However, liquidity remains under $100m with the expectation for this to drop tomorrow as repo sources (rebalancing) are reduced. . . .
>
> . . . .

[23] In his email, Steenkamp also referenced having left Corzine a voicemail and noted that he had been "catching-up" with Mahajan and Besgen "in detail" about the liquidity problems.

> However, Jon, more worrying is we need to address the sustained stress. In summary, we have three pools of liquidity for [MFGI] - (1) [F]in[C]o cash which is real and permanent, (2) FCM excess cash which is temporary and volatile, as depends on how customers post margin, and (3) the situation of our broker- dealer that is currently unable to fund itself, and more worrying continues to need more cash than we have in [F]in[C]o, thereby having us dip into FCM excess every day. This should be temporary but is becoming permanent, and the FCM cash is not reliable. Why is [the] B[/]D unable to fund itself? Part of it is the permanent pool of liquidity needed for [Euro RTMs], but we also see continued haircut increases in fixed income, increased funding needed for PSG and box size being permanently large . . . . [T]his continued liquidity stress is not sustainable without either more permanent (not temp) liquidity, or mitigating steps taken.

Corzine, Steenkamp, Abelow and others in management knew that all of the problems listed in the email existed well before Steenkamp sent the email on October 6. The Company's inability to rely on the unsecured RCF as a source of liquidity, the increased funding needed for PSG, and the growing size of securities "in the box," the temporary and volatile nature of FCM cash that made it an inappropriate source of sustained funding, the shrinking cash available for liquidity funding, the permanent pool of liquidity needed to fund the Euro RTMs, and the inability of the B/D to fund itself were topics that had been discussed and raised with and among management before October 6, 2011.

Subsequent communications continued to alert management to the fact that the Company's cash was drying up:

> (1) On October 11, 2011, Abelow and Steenkamp learned that the B/D was using $210 million of FinCo's $226 million liquidity pool;
>
> (2) On October 13, 2011, Abelow and Steenkamp further learned that FinCo's $233 million balance had been completely used by the B/D, which was already borrowing $34 million from the FCM;

(3) By October 14, 2011, Abelow and Steenkamp learned that the B/D was using $318 million from a combination of FinCo ($249 million), the FCM balance ($53 million), and the FCM buffer ($16 million), which consisted of funds held by the Company in customer accounts in excess of certain regulatory requirements;

(4) On October 14, 2011, Steenkamp described the Company's liquidity to Corzine as "very tight"; and

(5) On October 17, 2011, Steenkamp informed Corzine and Abelow that, instead of ending the day with positive amounts of cash, the Company had actually ended the day with negative $16 million. Due to a regulatory requirement that MFGI "lock-up" $19 million to meet potential customer demands, the Company would have a negative $35 million starting the following day.

As of October 17, 2011, MF Global was experiencing a significant stress on capital. Since the end of June 2011, the Company went from having excess cash and fully paid securities of $149 million to needing $318 million in cash. That increased funding need was due in part to a $179 million increase in Euro RTM margin calls which had increased from $248 to $427 million, as well as $126 million needed to finance the securities that were stuck "in the box," a funding requirement that had not existed as of June 30, 2011.

C. The Risks of the Company's Euro RTM Trading Strategy Materialize

1. The Company's Excessive Euro RTM Exposure

Corzine's bet on the Euro RTMs exposed the Company to an excessive level of risk. An October 2011 draft memorandum to the Board shows that the relative size of the Company's European sovereign debt exposure significantly outweighed that of other larger and better capitalized financial institutions. MF Global's exposure to European sovereign debt was more than four and a half times its equity, and 14% of its assets as of September 30, 2011, as shown in the table below, comparing MF Global's levels to those at other financial institutions:

Sovereign Exposure of Various Financial Institutions in October 2011

Company	Stated Balance Sheet Exposure	Exposure as a % of Q End Equity	Exposure as a % of Q End Assets	Quarterly VaR Average	VaR as a % of Q End Equity
MF Global	$6.4 B	460.6%	13.9%	$3 M	0.2%
Citigroup	$13.5 B	7.7%	0.7%	$184 M	0.1%
Goldman Sachs	$1.9 B	2.6%	0.2%	$101 M	0.1%
Jefferies	N/A	N/A	N/A	$12.7 M	0.4%
JP Morgan	$14 B	7.7%	0.6%	$94 M	0.1%
Morgan Stanley	$2 B	3.4%	0.2%	$145 M	0.2%

2. The Revolving Credit Facilities

The secured and unsecured RCFs were not intended as a permanent source of liquidity. Rather, in Corzine's own words, they were intended to serve as a backstop for extraordinary situations, "a liquidity pool and not a component of [the Company's] long-term capital structure."

Nevertheless, management increasingly viewed the RCFs as a safety valve for the Company's growing liquidity pressure. In Steenkamp's view, the Company had $2 billion in liquidity as a result of the RCFs, FinCo cash, excess liquidity around the world, and available client collateral. It is clear that the Company's RCFs were a significant basis of Steenkamp's view that the Company's balance sheet was secure. This view formed the basis of Steenkamp's assurances to the Board that the Company was able to meet its obligations, particularly during meetings where Corzine was seeking additional increases to the European sovereign risk limits.

Numerous Board members cited the CFO's assurances – from both Steenkamp and his predecessor, MacDonald – that all liquidity stress scenarios could be met as one reason that they agreed to Corzine's requests to increase the size of the Euro RTM portfolio. Steenkamp told the

Board that the unsecured RCF provided one means of satisfying all of the Company's liquidity needs.

Reliance on the RCFs ultimately was not enough. By August 11, 2011, the Risk Department had generated liquidity stress scenarios that Stockman presented to the Board showing a potential funding requirements of $1.43 billion. That amount would have exceeded the liquidity available under the Company's unsecured RCF alone.

3. MF Global's Liquidity Could Not Support the Euro RTMs

By August 2011, MF Global's lack of long-term liquidity was a serious threat to the Company's survival, a fact that should have been clear to those with knowledge of the Company's trading and funding positions, even with the limited and imprecise information available to them.

a. Impact of Initial and Variation Margin

As discussed above in Section II, the Euro RTMs required MFGI to fund Initial and Variation Margin calls. Initial Margin was set according to a formula: a highly-rated counterparty would be required to post a lower percentage of Initial Margin than a lower-rated counterparty. If a company were downgraded, additional Initial Margin would be imposed according to the counterparty's revised credit rating. Thus, if the sovereign issuer or MF Global's credit rating were downgraded, which ultimately occurred, MFG UK, and thereby MFGI, would have to satisfy potentially large increases in Initial Margin. Although large margin swings did not occur daily, the clearinghouses automatically debited such calls when they occurred.

MFGI also was subject to "super-margining" (*i.e.*, very large Initial Margins) on certain Irish and Portuguese Euro RTM positions, which stemmed from a combination of MF Global's

downgrade and its concentration in certain holdings. For example, if the Initial Margin were 3% and an additional 15% were added due to the European sovereign's credit risk, the Initial Margin charge would become 18%. These increments reflected the clearinghouse's best approximation of how certain bonds would be priced in the event of default.

In the event of a Variation Margin call, MF Global typically had a few days to comply with the demand. Variation Margin moved on a daily basis, depending on changes in the value of the underlying bond. For example, if a bond were worth $100 million and the value of the bond decreased by 1%, the Company would have to post an additional $1 million with the clearinghouse. Variation Margin is marked to market on a daily basis, meaning the same percentage move in the market translates to the same percentage increase in Variation Margin.

The margin calls on the portfolio were issued by LCH to MFG UK, which then sent requests for payment to MFGI. MFGI satisfied the margin calls by transferring cash or securities, usually U.S. Treasury bills. MFG UK also could demand advance margin funding from MFGI in anticipation of a margin call from LCH, pursuant to the GMRA. MFG UK invoked this contractual provision on at least one occasion during the last week of the Company's existence.

b. Growing Liquidity Pressure From the RTM Portfolio

The liquidity pressures caused by the Company's Euro RTM portfolio made it extremely difficult for the B/D to fund itself beginning as early as July 2011. The liquidity used to finance the margin on the Euro RTM positions essentially was trapped, because the Company could not unwind the Euro RTMs before maturity without taking a substantial loss. Management,

including Steenkamp and Corzine, was aware that the Company regularly drew on the B/D for liquidity to support the Company's Euro RTMs.

Investing so aggressively in Euro RTMs was an inherently unsustainable means of generating revenue over the long term because each new Euro RTM trapped liquidity for the duration of the investment. The Company had two options for increasing its revenue through these trades: one way was to increase the amount of the trades and the other was to extend the maturity date. Both of these courses increased the Euro RTMs' margin demands. At a certain point, the aggregate margin demands would exceed the Company's ability to finance these trades regardless of which option it selected.

The liquidity demands of the Euro RTMs became greater as Corzine extended the maturity date of the investments. When Corzine first entered into the Euro RTMs in September 2010, the maturity dates were either six, ten, or twelve months out. As discussed above, beginning in December 2010, Corzine began entering into larger Euro RTMs with longer maturities, some as long as twenty-one months. Thus, through the Euro RTMs, Corzine steadily increased the amount and duration of time in which MFGI's cash was tied up in the clearinghouses.

In this environment, Corzine and management understood the potential for disaster as a result of a stress event. In a meeting in his office with Mahajan in August 2011, Corzine showed Mahajan a Bloomberg article discussing how quickly stable funding sources at a B/D can disappear in a stress event. The article in question discussed, among other things, the effect of Lehman Brothers' bankruptcy on Morgan Stanley and how close Morgan Stanley had come to running out of cash as a result of a run on its prime brokerage unit, the unit that financed Morgan

Stanley's hedge fund trading and held its cash and securities. The article specifically warned against relying on brokerage accounts, which were susceptible to being closed on short notice by clients. Mahajan forwarded the article to Steenkamp.

c. Increased Margin Demands

The Euro RTMs drained MFGI's liquidity as MFGI struggled to find cash to meet the clearinghouses' margin calls. For example, in November 2010, a 15% haircut was imposed on some Irish bonds, resulting in an additional margin call from LCH. Similarly, on September 28, 2011, LCH issued a margin call for $440 million as a result of the change in value of certain Irish and Portuguese bonds.

Throughout the summer and fall of 2011, these margin calls persisted, locking up capital and dissolving the liquidity available to the Company. Risk scenarios presented to the Board on August 11, 2011 anticipated the need for as much as $930 million in additional funding to meet the Euro RTM margin calls.

LCH's margin announcements illustrate the increased liquidity constraints imposed by the Euro RTM positions. The Initial Margins on Portuguese and Irish positions began to increase materially at the time that Corzine started seeking risk limit increases from the Board. The Initial Margins associated with Irish and Portuguese positions reached 80% in the period between June and July 2011. Additionally, at various points in the winter of 2010 and spring of 2011, shortly after the Euro RTM strategy was initiated, LCH began refusing to accept various European sovereign bonds to satisfy margin requirements, making it more difficult for the Company to meet the calls.

Between July and September 2011, MFGI was forced to fund even larger margin calls at the clearinghouses. By the late summer and fall of 2011, as countries that Company management and the Board viewed as relatively safe investments were downgraded, the clearinghouses demanded additional margin:

(1) On July 14, 2011, Eurex made a $150 million margin call on Portuguese positions. (Those positions had been transferred from LCH to Eurex due to LCH's large Initial Margins, which eventually reached 80%.) Thus, as of July 14, 2011, the Portuguese margin requirement at Eurex was $181,561,623 million with approximately $106 million in Initial Margin and $75 million in Variation Margin;

(2) On September 6, 2011, there was a $33 million margin call related to the Company's Italian sovereign holdings;

(3) On September 13, 2011, there was another $28 million margin call related to the Italian sovereign holdings; and

(4) On September 20, 2011, there was a $20 million margin call related to the Company's Italian and Portuguese holdings.

In September 2011, Holdings Ltd. had to access the unsecured RCF to cover a $440 million LCH margin call relating to Irish and Portuguese bonds when end-of-quarter funding from Société Générale, a counterparty, could not be secured.

By October 17, 2011, MFG UK, and thereby MFGI, posted $275 million in Initial Margin at three clearinghouses: $99 million at Eurex for trades entered to offset the Irish and Portuguese Initial Margin; $168 million at LCH in Paris stemming from the Italian and Spanish RTMs; and $9 million at LCH in London.

During the last week before Holdings Ltd. and FinCo filed for bankruptcy, margin requirements on the Euro RTM positions increased dramatically and further stressed the Company's liquidity. Margin posted at the clearinghouses increased by $211 million to $663

million. The accelerated pace of the Euro RTM margin calls, coupled with other liquidity pressures experienced by the Company, ultimately caused MFGI to be unable to meet the margin calls received on October 31, 2011.

4. The Failure to Forecast or Effectively Challenge the Clearinghouses' Margin Calls

As Europe's economy worsened in the summer of 2011, Corzine asked the Treasury Department and Fixed Income trading personnel to provide additional detail on the reasons for increased margin calls, and often questioned the accuracy of those margin calls. Corzine wanted the forecasting data and also wanted a tool to challenge the clearinghouses' margin calls.

Despite the growing size of the Euro RTM portfolio, MF Global was not able to engage in reliable forecasting of Euro RTM margin calls, rendering the Company without the ability to manage this growing liquidity risk adequately or appropriately. Those at the Company responsible for these issues, including Corzine, accepted that such forecasting would not be available or forthcoming. For example, in a July 26, 2011 email chain among Besgen and other employees, Besgen wrote:

> I just had a conversation with Jon Corzine. He again asked what kind of forecasting we can do on the LCH/Eurex margin for the RTMs as well as clarity on the daily movements in the margin . . . .
>
> . . . .
>
> I need to have answers to the above even if they are not what JC wants to hear.

Two Treasury Department employees included in the email predicted that Besgen would not receive a response, indicating that it was common knowledge that such forecasting was not

available. Ultimately, Corzine and management failed to prepare for the margin demands that were an integral part of a Euro RTM portfolio the size of MF Global's portfolio.

5. Problems With MF Global's Hedging Strategy

MF Global's leadership also failed to execute a hedging strategy that effectively would reduce the Company's exposure to increasing margin calls in the summer and fall of 2011. Even as Stockman warned about the Company's growing exposure to the Euro RTM portfolio, Corzine and other members of management failed to reduce the Company's exposure by entering into any meaningful hedging transactions and continued placing long trades in European sovereign bonds after Stockman's July 2011 meetings. For instance, as of October 29, 2011, there were no short positions covering the Company's large exposure to Portuguese and Irish debt.

Corzine directed some hedging, but those positions were focused solely on reducing short-term margin calls from the clearinghouses rather than reducing effectively the Company's long-term exposure to liquidity drains from the Euro RTMs. By the late summer or early fall of 2011, the Euro RTM portfolio had grown to a gross figure of $11.7 billion, with approximately $3.5 billion in hedges, thus accounting for a net long position of $8.2 billion. Although the hedges decreased the size of the portfolio, they were not true hedges in the sense of offsetting risk. Rather, the hedging transactions only reduced margin requirements. The Company was hedging to reduce the amount of margin being demanded by the clearinghouses, not the market risk associated with the positions.

MF Global also entered into shorter term trades with the clearinghouses to reduce margin requirements, including short term RRTM and reverse repos that were not to maturity. RRTMs

were used to reduce Initial Margins on Irish and Portuguese bonds. In an email to Michael Wieczorek (MFGI's Head of Finance and Short Term Trading), Stockman and others, Mahajan wrote, "Jon C. emphasized today (for the second time this week) that he wants to see how we can optimize the margins being posted against our RTM trades by doing more reverse repo trades . . . ."

The hedging transactions were not always effective in accomplishing what Corzine wanted them to accomplish. For example, in one transaction, Corzine directed the Company to use a $1.3 billion short purchase of French bonds as a proxy hedge for the Company's exposure to Italy and Spain, even though the benefits of the trade were minimal as a result of LCH's netting rules. A Treasury Department specialist at MFG UK familiar with the trades concluded that the French trades created additional drains without necessarily netting Italian positions that may have already been netted through an Italian RRTM. Even though it was not clear that the hedge would have a positive effect and might only produce minimal liquidity, Corzine nonetheless proceeded with the French netting trades.

It appears that Corzine also used RRTMs to reduce the Company's net Euro RTM positions, which allowed him to accumulate gross long positions in excess of the risk limits set by the Board. These gross long Euro RTM positions ultimately reached approximately $12.5 billion in or about the end of July 2011.

Management also knew, as early as June 6, 2011, that the duration mismatch between the Company's long and short positions could lead to increased margin demands and liquidity pressure. In a June 6, 2011 email, Steenkamp wrote:

> [T]here could be an impact on the reverse RTM netting trades as these are to different maturities than the original RTM's. The

> potential issue is whether some counterparties will choose not to roll over transactions or the trading counterpart can't trade with us due to our rating. If this were to happen, then [MFGI] could lose its netting benefit on these reverses and thus be subject to higher margins, thereby increasing liquidity needs for the [B/D].

In the same email, Steenkamp noted that the failure to roll-off netting trades for certain Irish and Portuguese positions could lead to a combined liquidity requirement of approximately $313 million, which would probably require Holdings Ltd. to draw on the unsecured RCF. Despite their knowledge that short-duration RRTMs did not fully hedge the liquidity risks posed by increasing margin calls, neither Corzine, Steenkamp, Abelow, nor any other member of MF Global management acted to minimize the Company's overall exposure to long European bond holdings.

Towards the end of the summer and beginning of the fall of 2011, MFG UK's repo traders were having greater difficulty financing the Euro RTMs in the market, and the Company's counterparties, such as Société Générale, BNP, and certain Italian banks, were experiencing balance sheet constraints and refusing to roll over the short-term contracts back on their books the following month. As a consequence, the Company had to pay a higher price for these transactions.

At the close of the quarter ending September 30, 2011, Société Générale decided not to fund a period when some of MFGI's RTM transactions were rolling off, or maturing, between September 29 and October 3, 2011. As a result, MF Global had to meet a margin call of approximately $440 million. The Company financed the large margin call through Holdings Ltd.'s draw down of $500 million on the unsecured RCF. The Company used $440 million to cover the margin call and retained $60 million for the benefit of MFGI (in large part to cover the

capital charge imposed by U.S. regulators). When the Company renewed its financing arrangement with Société Générale and the margin was released, the borrowed funds were returned and the RCF was repaid.

6. Other Funding Pressures Affecting MF Global's Liquidity

a. PSG Trading Desks

MF Global's funding needs increased as the specialty trading desks within PSG became more active. Some positions held by various PSG desks were easy to fund, but others created significant challenges for the Company, particularly those involving less liquid securities, such as high yield corporate and distressed bonds. These less liquid investments began to pose greater funding pressure on the Company through the spring and summer of 2011.

Generally, the new proprietary traders hired by Corzine required large amounts of daily liquidity to fund their trading, and their activities ultimately had the effect of increasing the Company's liquidity stresses without producing any significantly improved revenues.

Many of the traders who joined the Company had little understanding of the Company's funding limits. These traders came from other financial institutions that were routinely capable of affording trades that were a stretch for MF Global. Although many of the traders were told when they were hired that MF Global would be challenged by some of these trades, the Company's management generally believed that the Company ultimately would be able to afford this kind of trading.

Beyond these liquidity challenges, the Company's increased proprietary trading also stretched the Company's capital resources. Capital Risk Incident Escalation reports circulated to management indicated decreasing levels of surplus capital almost daily during July and August 2011. Those reports informed management that the Fixed Income, equity, PSG, asset-backed

securities and mortgage-backed securities desks were extensive users of the Company's capital, sometimes dramatically exceeding their assigned capital limits.

For example, on August 25, 2011, a Capital Risk Incident Escalation report indicated that the Fixed Income proprietary trading desk used $214.2 million of capital against a $75 million limit, while the Equity proprietary trading desk used $27 million in capital against a $10 million limit.

Despite these warnings, management failed to ensure that individual traders were aware of the capital limits imposed on their group's or desk's trading, and the Company failed to implement a system to monitor real-time capital utilization or breaches.

Corzine recruited traders who traded securities that the B/D could not finance without drawing on the Company's own resources (securities "in the box"). From early 2011 through the summer, MF Global moved from having no securities "in the box" to an increasingly long list of such securities. By October 2011, the value of the box securities exceeded $100 million. At Corzine's request, the repo desk within the Treasury Department began putting together a list of securities "in the box," since it was understood that they were a growing drain on liquidity. Discussions about how to manage these securities grew more common, particularly among management, including Dunne, Steenkamp, and Corzine, although their discussions often revolved around how to fund them rather than considerations of whether to cease accumulating them or divest the Company of them.

By the late summer and early fall of 2011, meetings to discuss the box securities were occurring on a weekly basis. Corzine discussed the size of these securities, the drag on liquidity that the box securities represented, and explored options to finance them. Corzine was familiar

enough with each of the box securities to recognize daily movements and was focused during these discussions on optimizing short-term liquidity.

b. The HTM Portfolio

Corzine was closely involved in handling and overseeing the HTM portfolio, which also contributed to the Company's liquidity drains. Besgen managed the portfolio, obtaining repo funding through the B/D for every position bought into the HTM portfolio.

Under CFTC Rule 1.25, customer funds could be used to invest in certain assets. Besgen used those customer funds to invest in the HTM portfolio. He relied on O'Brien, her staff, and Serwinski to tell him how much money was available for investment in the HTM portfolio. He also relied on O'Brien to provide guidance on what types of investments qualified under Rule 1.25.

Initially, the HTM portfolio did not include investments in corporate bonds because they were eligible for Rule 1.25 investment only under certain conditions. The Company initially did not buy *any* securities that were not eligible under Rule 1.25 for the HTM portfolio, including the higher-yielding agency debt, because of the Company's own risk limits and the higher liquidity risks these securities represented. Because non-eligible securities had a lower rating and a lower probability of being funded, they would provide an increased risk to the Company that it would not be able to obtain funding on those assets. By excluding riskier securities and focusing on agencies and U.S. Treasuries, there was little liquidity risk because, even if Rule 1.25 funds were not available, there was a liquid market for those instruments.

Corzine changed the HTM portfolio by increasingly investing in securities that were less qualified or not qualified for investment of FCM funds. Corzine also set the strategy for

increasing risk limits for the HTM portfolio. He sought increases to the limits to take advantage of higher yields. Besgen would compile lists of available corporate bonds, and Corzine would select from that list the bonds in which he wanted to invest. Over the course of Corzine's tenure at MF Global, the HTM portfolio was converted steadily into a book of corporate bonds, a growing portion of which was being financed without funds from the FCM. This increase in the HTM portfolio's size further contributed to the Company's liquidity challenges because the Company primarily funded the HTM portfolio holdings through repos, which required additional margin and additional liquidity.

The HTM portfolio increased from approximately $5.5 billion to $10 billion just prior to Holdings Ltd. and FinCo's bankruptcy filings, when Holdings Ltd. liquidated almost 90% of the HTM portfolio. Rather than face the growing pressure the box securities were putting on the Company's liquidity and reduce the HTM positions, Corzine was often more focused on optimizing liquidity, or finding ways to maintain the positions, despite the liquidity stress they created.

7. The B/D's Growing Reliance on the FCM for Funding

As the Company's liquidity pressures increased as a result of Corzine's trading strategy, the B/D increasingly turned to the FCM to meet its growing demands for cash. For at least a year prior to MF Global's collapse, the FCM provided cash through intraday transfers to the B/D, often in amounts between $50 and $100 million. The transfers were approved by O'Brien or other Treasury Department employees in Chicago. The transfers often occurred on an ad hoc basis, without planning or forecasting.

Due to its lack of controls, the Company was unable to identify the specific areas or trades that were driving the need for the intraday transfers. As a result, the Treasury Department was forced to approve intraday transfer requests from the B/D without adequate information or forecasting. The Company also lacked a formal process for documenting the approval of intracompany transfers from the FCM to the B/D.

An example of the undisciplined nature of these transfers occurred when Dominick Delucia, a Vice President in the Operations Department "back office" in New York, sought a $100 million transfer late in the day on July 26, 2011. O'Brien approved the transfer and asked the Treasury Department to facilitate the movement of cash. According to O'Brien's email, Serwinski "was not pleased about the late hour borrow, nor the size," as excess segregated funds were only $127 million at the time. Frustrated at the circumstances and the B/D's inability to manage its intraday cash, she reacted, "What if I say no? What if they needed 150mm and I only gave them 100mm?"

This incident revealed the absence of planning, advance notice, and a reliable approval process for these transfers.

8. Methods Available for Calculating Segregated and Secured Funds

As a regulated entity, MFGI had two available methods for calculating the amount of funds that needed to be kept in the secured environment for assets on deposit in foreign secured accounts: the "**Alternative Method**" and the "**Dollar-for-Dollar Method.**" MF Global used the Alternative Method, which always generated a lower secured dollar amount than the Dollar-for-Dollar Method.

The Alternative Method is computed on a customer account by customer account basis, and only includes the value of each customer's open positions, not cash, that is the sum of an account's risk maintenance margin requirement, open trade equity, and securities and net options value. This results in a significantly lower secured margin requirement as compared to the Dollar-for-Dollar Method because, in effect, it omits the value of cash held in accounts without open trade positions.

Use of the Alternative Method meant that MF Global could remain in regulatory compliance while keeping a significantly lower balance in its foreign secured accounts than would be required if the Company used the Dollar-for-Dollar Method. For example, if a customer gave the FCM $100, but took no positions, under the Dollar-for-Dollar Method, $100 would be kept secured. Under the Alternative Method, because there were no open positions, there would be no need to secure funds.

MF Global's predecessor entities had used the Dollar-for-Dollar Method until 2005, when Refco was folded into the business. Under then-CFO MacDonald, the Company revisited this accounting methodology again in 2009 after the Dooley incident, but elected to continue using the Alternative Method despite the risks inherent in this approach.

9. Use of the Regulatory Excess

When the change to the Alternative Method was made, the Financial Regulatory Group decided to calculate the foreign secured requirement based on the Dollar-for-Dollar Method as well, with the difference between the two calculations called the "Regulatory Excess." Even though it was permissible to use excess secured funds outside the regulated environment, MF Global adopted a policy not to take excess customer funds outside the FCM.

In July 2011, management, including Corzine and Steenkamp, began to look into how much of the FCM's Regulatory Excess funds could be drawn on to fund the B/D business on a regular basis. The Company began to rely increasingly on these funds during the summer and fall of 2011 as a regular source of liquidity due to the B/D's inability to fund its own operations. During a telephone conference with Treasury and Finance Department personnel in July 2011, Steenkamp suggested that there was a proposal to utilize excess segregated funds to support B/D investments.

Serwinski later called Steenkamp to express her discomfort with the idea that FCM funds would be used by the B/D on a regular basis. She understood that Steenkamp was seeking information to provide to Corzine, and Steenkamp pressured her to get the issue resolved. On July 20, 2011, Serwinski emailed O'Brien and Hughey, asking them to confirm the information she was preparing for Steenkamp. Hughey computed the monthly averages for the Excess Segregated and Excess Secured amounts for the period July 1, 2010 through June 30, 2011 and found there were "five instances where the [Company] was funded by clients (*i.e.*, the excess contributed by [the Company] was negative)." Four of the five instances were consecutive days: "12/01/10 ($98.0 million), 12/02/10 ($38.0 million), 12/03/10 ($19.4 million), and 12/04/10 ($19.4 million)." Hughey asked Serwinski: "Do we have any idea what happened . . . to cause these? I would think Henri would ask that question."

Although the FCM had provided funding to the B/D in the past, management's proposal appeared to be a plan to use customer funds as a source for trading on a regular basis. The request also came at a time when the FCM's excess funds had eroded from approximately $150 million to $75 million.

Steenkamp asked Serwinski to provide "trend data," including highs and lows of amounts held in the regulated environment. Serwinski provided the information in a July 27, 2011 email to Steenkamp, stating that she understood "the working capital (liquidity) situation the [Company was] facing." Serwinski also stated her concerns that (1) FCM client assets would be put at risk even if only overnight, (2) the FCM client asset base "should not be a [B/D] working capital source strategy to be relied upon," and (3) "[i]n the event of a financial crisis, [was MF Global] guaranteed that [it] could draw down on the [unsecured] RCF to meet the [Company's] liquidity needs and return the FCM client assets to meet any requirements in the seg/secured environment?"

Serwinski suggested that Steenkamp contact counsel immediately to ensure that this strategy "is not violating any fiduciary obligation to our customers." Serwinski made clear to Steenkamp that she "professionally [did] not agree with the concept of using FCM customer funds to provide liquidity to the House [B/D] investment and trading."

In response to her email, Steenkamp stated: "[B]ased on the lows, that means that technically speaking, the low of $433 m[illion] is probably what we should max out as available client excess liquidity available to [the B/D] . . . ." Steenkamp also stated that, "Global liquidity needs is what the committed RCF is available for."

After consulting with others at MF Global, as well as two outside law firms, Serwinski reduced her concerns to a memorandum. The memorandum concluded that there were no laws or regulations that prohibited the proposal to lend up to $250 million in excess funds to the B/D on an overnight basis. However, the memorandum also concluded that, as a result of Rule 15c3-3, under the Securities Exchange Act of 1934, the Company would have to lock up any portions

of client balances not included in the regulated environment at month's end. As a result of the lock-up performed each month, Serwinski concluded the proposal to use excess client fund balances "does not appear to be an optimal solution for meeting [B/D] liquidity needs."

Despite Serwinski's repeated caution against this strategy for meeting the B/D's liquidity demands, Steenkamp advised Serwinski and others that he had:

> walked [Corzine] through the education you all gave me . . . . He gets the concept of lock-up — and agrees that we have to comply with that. However, as part of overall liquidity management, he would like to know how we can use all surplus daily (even if only $50 [million]), maximize it through daily liquidity management and also use other securities to fund the lock-up. He also understands using other securities would have a cost, but is looking for this group to come to him with solutions/options, and also accompanying costs.
>
> When do you guys think you will be able to get back to [Corzine] with a more definitive answer and recommendation?

Corzine and Steenkamp persisted in their attempt to use FCM funds to meet growing B/D liquidity pressures in the summer of 2011. Although Besgen responded that he would look into the issue, it does not appear that Serwinski or her staff offered any additional suggestions to Steenkamp and Corzine.

The debate surrounding greater reliance on the FCM funds by the B/D, the B/D's growing use of intraday transfers from the FCM, and the increased liquidity pressure that caused the B/D to rely on the FCM was unknown to the Board through the summer of 2011. There were no discussions with the Board about the B/D having difficulty funding itself. Indeed, the B/D's liquidity issues were not even discussed with the Board when Corzine reported on the progress of his four to six quarter strategy to move the Company to a full scale investment bank.

Board members did not believe that the Company was experiencing any significant liquidity pressures during the summer and fall of 2011. They were not informed of any such issues or the fact that the B/D was borrowing from the FCM. They were not aware of discussions about Corzine's exploration of possible uses of FCM funds.

IV. CONCLUSION

On October 25, 2011, six days before the Company collapsed, its CFO, Steenkamp, told the investing public:

> [D]uring times of market strays, you have the opportunity to test many aspects of your businesses, including risk system, processes, people, and our capital and liquidity assumptions as well as operational controls. While our financial performance may not have demonstrated our full potential, I can tell you with confidence that our functional areas, including risk, operations and treasury, performed exceptionally well.

Steenkamp may have been correct that times of crisis test a company's functional areas, but he was wrong in his assurance that MF Global's Risk, Operations, and Treasury Department systems would survive regulatory scrutiny, downgrades, increased margin calls, a media frenzy, and a run on the bank.

Corzine's trading strategy involved taking positions in various commodities, securities, and other instruments or products either to facilitate client trades or "to monetize" – that is, attempt to profit on – the Company's views on future market price movements and volatilities. This strategy was a decisive and profound change in the Company's traditional business model. In less than a year, the Company's Euro RTM positions increased from less than $400 million in mid-September 2010 to an almost $8.3 billion net position at the end of August 2011.

Even as the Company embarked on a path to alter its business substantively, structurally, and operationally, management ignored operational and risk deficiencies in the Company's

controls that could not sustain this transformation. Despite having written policies in place after the near disaster caused by the Dooley incident, the Company's controls remained defective in practice. In the end, the scale of the Company's trading put pressure on the Company's deficient controls without producing any significantly improved revenues.

Corzine and his management team were fully aware of the limitations of the Company's systems, the growing pressures the Company was facing as a result of its trading strategy, the demands of its regulators, and the worldwide economic situation. The decision to expand MF Global's proprietary trading may have appeared sound in a vacuum, but in the reality of the business Corzine and his management team inherited with its known controls and resource deficiencies, this strategy was disastrous.

Disaster struck during last week of October 2011. Capital and liquidity assumptions driving the Company's trading strategy were fatally flawed. During this time of crisis, MF Global needed to rely on its Operations, Risk, and Treasury Department systems. Those systems, however, were fatally flawed, even though Corzine and other members of his management team knew about their deficiencies many months before they were stretched to their limits. These defects, and management's failure to address them, contributed to the Company finding itself in a "run on the bank" scenario and ultimately spelled the Company's demise.

Based on the Trustee's investigation, the actions and failures of key members of MF Global's management, in particular the former Chairman and CEO Corzine, the former COO Abelow, and the former CFO Steenkamp contributed to the losses suffered by Holdings Ltd. and FinCo, which the Trustee estimates to be between $1.5 billion and $2.1 billion.[24]

[24] An analysis of the Trustee's loss calculation is attached as Appendix E. Additional support for the loss calculation is attached as Appendix F.

* * * *

In accordance with his duties under 11 U.S.C §§ 1106(a)(3) and (a)(4)(A), the Trustee offers this Report of the investigation conducted into the events and circumstances that ultimately led to Holdings Ltd.'s and FinCo's bankruptcy filings on October 31, 2011.[25]

Dated: April 3, 2013
New York, New York

Respectfully submitted,

/s/ Brett H. Miller

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[25] The Trustee has prepared a complaint against former executives alleging breaches of fiduciary duty. After discussions with the Hon. Daniel Weinstein, the mediator appointed in *Deangelis v. Corzine et al*, Case No. 11-cv-07866-VM (S.D.N.Y), the Trustee has agreed to postpone the filing of the complaint pending the completion of the mediation.